INDUSTRIAL ENTERPRISE IN INDIA

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INDUSTRIAL ENTERPRISE IN INDIA

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PREFACE TO THE FIRST EDITION

IN RECENT YEARS many writers have written excellent treatises on the development and organization of the various industries in India, but in very few of these studies has sufficient attention been paid to the details of their organization. The important activities of the managing agents, who virtually dominate industrial enterprise in India, their functions as the main providers and guarantors of industrial finance, their recent malpractices and abuses and, finally, their conflicts with shareholders and directors are subjects which need to be carefully studied by everyone interested in the industrial development of India. In the present work, an attempt has been made to cover these rarely discussed matters as also the allied subject of mushroom and fraudulent companies. I have also dealt with the recent phenomenal growth of private joint-stock companies and the economic significance of the provisions of the new Indian Companies' Amendment Act. How far my study fills up a gap in the recent economic literature on these subjects, it is for my readers to judge.

To some extent this book is a sequel to my earlier work published last year, *Banking and Industrial Finance in India*. In that book, I studied the development of modern banking institutions in India from an entirely new and objective angle and with special reference to the needs of industry and trade. In the present work, the part that Indian banks can and should play in the matter of financing industrial enterprise in India has been considered in detail and, as before, from a purely economic standpoint. Further, I have attempted to bring out the intimate connexion that subsists in India between the problems of industrial management on the one hand and those of industrial finance on the other.

In conclusion, I should like to express my deep gratitude to the authorities of the University of London, who gave me special permission to complete this work within a short space of four months and after a long absence of four years in India. I am also grateful to my teachers Prof. Lionel Robbins and Dr. Vera Anstey of the London School of Economics, for their valuable help and guidance. I must also mention the

various Chambers of Commerce and Shareholders' Associations in India, who very kindly supplied me with copies of their carefully prepared memoranda on the Indian Companies' Act (Amendment) Bill, 1936, and who also replied to a number of questions put by me to them. I only hope that this book will be of at least some use to them.

N. Das

London School of Economics
and Political Science
May 1937

PREFACE TO THE SECOND REVISED EDITION

THIS BOOK went out of print in 1948, and since then I have been receiving requests from many quarters to bring out a revised and up-to-date version of it. I could not, however, undertake the work for some time, mainly because of the uncertainties about the future of company management and administration in this country. It was only when the new Companies Bill was finally passed by the Indian legislature that I could direct my attention to the work of revision.

As I started on the work, however, I found that mere revision would not meet the situation. Not only had the facts and circumstances changed considerably since the book was first published in 1938, but the entire economic and social landscape had undergone a transformation, almost beyond recognition. I, therefore, had to completely rewrite the book. Those who have in their possession a copy of the first edition of this book will, I fear, find that the present edition represents an entirely new book.

I should like to take this opportunity of expressing my deep gratitude to the different Chambers of Commerce and Industry & Associations who have ungrudgingly placed at my disposal the memoranda or notes they had submitted to various Committees and Commissions set up by the Government of India since 1947. Thanks are also due to the Research and Statistics Division of the Department of Company Law Administration in the Ministry of Finance, Government of India. I have freely drawn upon the excellent monthly and annual reports published by this Department. I should like to add, however, that the views expressed herein are exclusively mine and should not be taken to reflect those of the Department of Company Law Administration or of any other organization of Government.

N. Das

Calcutta
April 1956

PREFACE TO THE THIRD REVISED EDITION

THE SECOND REVISED EDITION of this book was published in April 1956, coinciding more or less with the coming into operation of the new Indian Companies' Act and also the beginning of the Second Five-Year Plan. Since then, the country has had an opportunity of assessing and evaluating the impact of the Act on industrial enterprise. The Second Five-Year Plan has also been completed and the Third Five-Year Plan has just begun: there has occurred a tremendous economic upsurge during the period 1956-61. I, therefore, thought it fit to revise the book afresh, incorporating in it all the latest facts and data and highlighting the new trends, especially developments in the so-called public sector. Attention is particularly invited to the three new chapters I have put in, viz. those relating to *Concentration of Economic Power*, *Problems of Management*, and *Company Finance and Profits*. I only hope that this third revised edition will receive from the public as generous a reception as the two previous ones did.

In revising the book, I have drawn freely upon the reports and memoranda issued by the Department of Company Law Administration, Government of India, New Delhi, and the bulletins published by the Reserve Bank of India, Bombay. To both these organizations I express my deep gratitude. I am also thankful for the assistance I have received from my colleague Mr. P. Y. Chinchankar, in checking up the Statistical Tables and other relevant data. Finally, I must express my gratitude to my Secretary Eva D' Silva for the care she has taken in preparing the typescript, re-arranging the new material I have incorporated in this book and generally keeping up with the high tempo at which I worked.

N. Das

Bombay
April 1961

PREFACE TO THE FOURTH REVISED EDITION

THE LAST REVISED EDITION had such a generous reception from the public that it was exhausted in less than a year and it became necessary to bring out a fresh edition.

To be really useful, a book of this kind must give the latest facts and figures. Accordingly, I have taken this opportunity to bring all the relevant information and data (including the Tables in the Appendix) up to date.

N. Das

Bombay,
June 1962.

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CHAPTER I

THE DEVELOPMENT OF MODERN INDUSTRIAL ENTERPRISE IN INDIA

The Beginning

THE DEVELOPMENT of modern industrial enterprise in India is not more than a century old. It is true that a few industrial undertakings were started in the first half of the nineteenth century—by British capitalists in the Bengal Presidency and by some Indian merchants in the province of Bombay, but they were more or less pioneer undertakings started in a rather haphazard fashion and none of them presented the intricate problems of modern capitalistic enterprise—the problems of finance and management.

Even in Western India, most of the industrial enterprise was dominated by the British. Contrary to popular belief, the cotton mill industry of Bombay and other parts of the country was not exclusively Indian, looked at from any point of view—whether financial, personnel or ownership. The first cotton mill was put up in India in 1817 by an Englishman, but it failed. The Fort Gloster Mill was put up in 1830 in Bengal under European management. C. N. Davar's mill in Bombay (established in 1854) was partly owned by Englishmen. Killick, Nixon & Co., a British firm of managing agents, laid the foundation-stone of their Kohinoor Mill as early as 1870. Even in later days, we find the Sassoon, Greaves and Cotton, Bradley and Brady interests dominating the industry in Bombay, and the Harveys, Staneses and others setting up cotton mills in Madura, Coimbatore and Cawnpore.[1] As regards the jute and tea industries, they were exclusively European to start with, and so were the coffee and sugar plantations.

The reasons for this state of affairs were obvious. The traditional industries and crafts of India had declined—partly owing to the impact of machine-made goods and partly owing to the deliberate pursuit of a policy to retain India as a permanent market (almost a dumping ground)

[1] S. D. Mehta, *The Indian Cotton Textile Industry*, Bombay, 1953.

for articles manufactured in the U. K. In due course, there was some relaxation of this policy, because it was found that there were some local raw materials which could be processed more economically inside the country than be exported as such to the U. K. Moreover, her economic hold over India having been well secured, the Government could afford to make a few minor concessions. And, when relaxation came, it was the British merchants with their connexions (and sometimes head offices) in the U. K. who were in a better position to take advantage of the situation than the Indian business community. Secondly, the latter were generally apprehensive of embarking on new ventures and part at least of their apprehension arose from the fact that economic policy was still dictated by British interests in the mother country.[1]

The Swadeshi Movement and After

The year 1905 was a turning period in the history of industrial enterprise in India. The partition of Bengal, announced by Lord Curzon, led directly to the Swadeshi movement urging the boycott of foreign goods and the use by consumers of articles produced locally. The industrial consciousness of the people was stirred to a phenomenal degree almost overnight and there was a great outburst of industrial promotion by Indians themselves. The number of joint-stock companies registered in India rose from 1,340 in 1900 to 2,744 at the outbreak of World War I, and the paid-up capital increased from Rs 34.7 crores to Rs 76.6 crores.

As more and more people turned ther attention towards the promotion of new industrial ventures, difficulties began to be encountered. Throughout the three decades between 1920 and 1950, we find entrepreneurs complaining that capital was shy and inadequate both for the launching of new enterprises and for the development of existing ones, and, for this, they blamed the apathy of the general body of investors and the conservative policy pursued by the various banking institutions. Investors and the general public, on the other hand, retorted that it was the defective manage-

[1] For a very exhaustive historical survey, the reader is referred to the author's *Banking and Industrial Finance in India,* Calcutta, 1936, Chs. II-VII.

ment of industrial enterprise which was at the root of all the trouble. Echoes of these two conflicting statements can be heard even today, when industrial production has reached a new all-time peak, rapid technological progress has been achieved and production patterns have also altered almost beyond recognition.[1]

Let us, however, go back to the period 1914-47, i. e. the period between the outbreak of World War I and the attainment of independence by India. The impact of World War I on the industrial development of the country was not inconsiderable. Towards the middle of the war, the British Government realised that an industrially developed India could have been of greater use to them even from the limited objective of winning the war. Special attention was, therefore, paid to the development of selected industries and an Industrial Commission was appointed in 1916 to conduct a comprehensive survey of resources and industrial possibilities. The Indian Munitions Board was set up in 1917 to foster the development of certain types of industries and, as a result, several new industries were started and many existing ones were further developed and extended.

As soon as the war ended, however, the new interest displayed by the rulers of the country flagged and even the halting recommendations made by the Indian Industrial Commission were shelved. The net result was that 'beyond affording temporary gains to a few well-eatablished industries, World War I did nothing to set the country firmly on the road to industrialisation. After 1918, the few industries which had been established on account of the war either stagnated or decayed; they could not face the competition from advanced industrial countries.'

The inter-war period (1918-1939) was also marked by the lack of a positive and vigorous policy. It is true that the Fiscal Autonomy convention was adopted by the British Parliament in 1921, so that India could follow an independent fiscal policy, but the 'independence' granted was hedged in by a number of restrictions. The same year, an Indian Fiscal Commission was appointed to recommend a suitable

[1] See, for example, P. A. Wadia and K. T. Merchant, *Our Economic Problem*, Bombay, 1960, Chs. XXIV-XXVI.

fiscal policy and, on the recommendation of this body, the Government of India adopted the doctrine of 'discriminating protection'. This was a step forward, in as much as, from this time onwards, the State ceased to be a disinterested spectator and committed itself to helping industries by the grant of protection in appropriate cases. In the years that followed, the Indian Tariff Board recommended, and the Government of India agreed to, the grant of protection to a number of industries, of which the most important were iron and steel, cotton textiles, sugar, paper and paper pulp, and match industries. But the Commission had laid down three rigid conditions which an industry had to satisfy before it could be granted protection. These were that (*a*) the industry must be one possessing natural advantages such as an abundant supply of raw material, cheap power, a sufficient supply of labour or a large home market; (*b*) the industry must be one which, without the help of protection, either was not likely to develop at all or was not likely to develop as rapidly as was desirable in the interests of the country; and (*c*) the industry must be one which would eventually be able to face world competition without protection.[1] In the actual application of these conditions, the Government of India was even more rigid than the Tariff Board. Not infrequently, the former turned down the recommendations made by the latter—on the ground that the Board had not given due attention to all the three 'requirements' of the new fiscal policy.[2]

As has been aptly pointed out by a later commission (the Fiscal Commission of 1949-50), there was a fundamental defect in the approach of the Indian Tariff Board to the problem of protection. 'Protection was not visualised as an instrument of general economic development, but was viewed as a means of enabling particular industries to withstand

[1] This is how the Indian Fiscal Commission summed up their general attitude towards the quantity and quality of protection to be given: 'The protection we contemplate is a temporary protection to be given to such industries as will eventually be able to stand alone.'

[2] For example, the Government of India refused to accept the Tariff Board's recommendations for granting protection to glass and the worsted sections of the woollen industry on the ground that the essential raw materials were not available in the country. Similarly, the locomotive manufacturing industry was denied protection in 1924 on the ground that the home market was not large enough.

foreign competition. This resulted in a somewhat lop-sided development, With such an approach, it was not possible for basic and key industries to develop. It is also likely that the protection of isolated industries without a positive effort being made at the same time to provide facilities for the establishment of allied industries added to the total burden on the community.'[1]

The result was that India remained industrially backward even on the eve of the outbreak of World War II. Barring the growth of a few consumers' goods industries (the iron and steel industry was the only exception), there was practically no development in the sphere of capital goods industries. Although India had become a permanent member of the ILO as one of the twelve States of major industrial importance, her economy was weak and her industrial development lop-sided. This was reflected in the figures of workers employed in industries, returned under the Factories Act. Between 1897 and 1914, the number of industrial workers had increased from 421,000 to 951,000, but between 1922 and 1939, it had increased from 1,361,000 to only 1,751,000. Secondly, while India had become independent of foreign countries in respect of sugar and cotton goods and was able to meet part of her requirements of cement and iron and steel from her own production, she was still largely dependent on them for the offtake of a substantial part of her production of raw materials. What was worse was that she had to depend almost entirely on these countries for the supply of machinery and other capital goods. Even the *Economist* of London, in its survey of Indian industrialisation at the end of 1936, observed: 'Although India has begun to modernise her industries, it can hardly be said that she is as yet being industrialised.'[2] Another disinterested observer remarked as follows in 1934: 'With abundant supplies of raw cotton, raw jute, easily mined coal, easily mined and exceptionally high

[1] *Report of the Fiscal Commission*, 1949-50, Vol. I, New Delhi, 1950.

[2] It is true that the number of joint-stock companies registered in India and at work increased from 4,708 in 1921 to 11,114 in 1939 and the paid-up capital from Rs. 164.5 crores in 1921 to Rs 290.4 crores in 1939, but these figures include banking, loan and insurance companies, trading companies and land and building companies. If the figures for these latter be excluded, the increase works out from 1,701 companies with a paid-up capital of Rs 76.1 crores in 1921 to 3,278 companies with a paid-up capital of Rs 154.7 crores in 1939.

grade iron ore; with a redundant population often starving because of lack of profitable employment; with a hoard of gold and silver second perhaps to that of no other country in the world, and with access through the British Government to a money market which was lending large quantities of capital to the entire world; with an opening under their own flag for British business leaders who were developing, both at home and in numerous new countries. all sorts of capitalistic industries; with an excellent market within her own border and near at hand in which others were selling great quantities of manufactures, with all these advantages India, after a century, was supporting only about two per cent of her population by factory industry.'[1]

Meanwhile, the Working Committee of the Indian National Congress had formulated (in August 1937) a definite policy with regard to industrial and social planning. They recommended to the Congress Ministers, who had assumed power in most provinces, the appointment of a committee of experts 'to consider urgent and vital problems the solution of which was necessary to any scheme of national reconstruction and social planning.' It was emphasised that such a solution would require extensive surveys and collection of data, as well as a clearly defined social objective. In July 1938, it was decided, as a preliminary step, to convene a conference of the Ministers of Industries of the various provinces and call for a report on the existing industries operating in different provinces and the needs and possibilities of developing new ones.

This conference was held in Delhi in October 1938, and the thesis was laid down that the problems of poverty and unemployment, of national defence and economic regeneration in general, could not be solved without industrialisation. It was decided that, as a step towards such industrialisation, a comprehensive scheme of national planning should be drawn up—a scheme providing for the development of heavy key industries, medium-scale industries as well as cottage industries, keeping in view the requirements, resources and peculiar circumstances of the country. With a view to giving effect to the above policy, a National Planning Committee

[1] D. H. Buchanan, *The Development of Capitalistic Enterprise in India*, New York, 1934.

was set up. The Committee started functioning almost immediately, but World War II broke out and India was dragged in as a co-belligerent. All the Congress Ministries in the Provinces tendered their resignation by way of protest and many of the leaders were put behind prison bars. The work of the National Planning Committee was, therefore, held up.

World War II and the Post-War Period

The outbreak of World War II found the Government of India almost unchanged in its general attitude towards the development of industries. As the war progressed (particularly after Japan's entry into it), however, Government felt that India should develop as speedily as possible into an industrial arsenal for the Allied forces. The fall of France and the bombing of British ships and the Japanese penetration into the Southern Pacific demonstrated the dangers to an empire with widely scattered lines of communication. India and Australia were accordingly chosen as the centres of supply. By the end of 1941, pig iron production had increased from 1,600,000 tons in 1938-39 to 2,000,000 tons. Finished steel production increased from 867,000 tons in 1939 to 1,400,000 tons in 1942. A big programme was initiated in 1941 for the expansion of armaments works, explosive plants and small factories. Forty-four firms were licensed to manufacture machine tools, lathes, drilling, shaping and planing machines, furnaces and power blowers. Over 280 new items of engineering stores were being manufactured in India, ranging from small tools and machine parts to heavy calibre guns, torpedo boats and degaussing cables. There was a considerable expansion in the production of drugs, leather manufactures, hardware, glassware, cutlery and optical goods, and the beginnings of a heavy chemical industry were laid in 1941, resulting in the production of sulphuric acid, synthetic ammonia, caustic soda, chlorine and bleaching powder. The value of exports of manufactured articles rose from Rs 47.6 crores in 1938-39 to Rs 81.2 crores in 1940-41. In 1940, the Commerce Member of the Government of India announced that industries started during the war would be adequately protected if they were organised on sound business lines.

Nevertheless, even during the closing stages of the war, British policy was opposed to any *rapid* growth of heavy industries *controlled and managed by Indians*. Secondly, the very conditions created by the war had some adverse effects on industrial development in the immediate post-war period. The capital equipment of almost all industries had been strained to the maximum during the six years of the war. Many factories were working extra shifts and there was a continuous deterioration of plant and machinery, due to want of proper maintenance and replacement. The result was that when the war ended, most of the industries found it difficult to undertake large-scale replacement of worn out plant and machinery.[1] The following figures of industrial production between 1938 and 1946 tell their own story:—

Index of Industrial Production
(1937=100)

	General Index	Cotton Textiles	Jute	Steel	Chemicals	Cement
1938 ..	105.4	109.9	98.3	108.0	84.4	124.8
1939 ..	102.7	104.3	92.4	125.0	103.9	152.9
1940 ..	109.9	103.6	96.1	125.5	133.3	152.1
1941 ..	117.8	114.8	92.4	131.1	153.2	185.8
1942 ..	111.2	102.0	99.5	136.7	138.7	194.5
1943 ..	117.0	117.0	84.4	141.5	138.6	188.4
1944 ..	117.0	122.9	86.7	139.6	126.3	182.1
1945 ..	120.0	120.0	84.4	142.9	134.1	196.5
1946 ..	109.0	101.9	84.6	130.0	111.2	181.1

In other words, the increase in industrial output was only about 20 per cent during the period of World War II.

The post-war period (1945-1947) saw a steady falling off in industrial *production*. To some extent, this was inevitable, as demand arising out of war efforts had suddenly come to an end. But industrial *activity* did not suffer any setback. The number and paid-up capital of joint-stock companies registered and at work in India actually increased from 14,859 and Rs 389 crores respectively in 1945 to 21,853 and Rs 478.7 crores in 1947. Even excluding the figures

[1] The position in Australia was different. Although Australia served as the other important industrial arsenal for the Allies, a watchful and democratically elected Government saw to it that equipment and machinery were not strained beyond manageable proportions. Secondly, such industries as might be easily converted into civilian production at the end of the war were deliberately excluded from India's share in the war effort.

for banking, loan and insurance companies, trading companies and land and building societies, the picture was one of steady progress.

Developments after 1947

The attainment of independence by India on 15 August 1947, however, made a tremendous difference to the industrial landscape.[1] India was at last completely free to mould her economic destiny in any way she liked: indigenous enterprise was no longer required to function as the camp-follower of foreign interests.

The first three years of independence (1947-50) were, however, marked by various kinds of experimentation. The scars left by the stresses and strains of the war and of the partition of the country had to be attended to first. The new Government was, however, determined to make a frontal attack on the economic and industrial front as early as possible. So, in April 1948, came the famous Industrial Policy Statement, enunciating the respective roles of State and private enterprise. 'A dynamic national policy must be directed to a continuous increase in production by all possible means, side by side with measures to secure equitable distribution. The problem of State participation in industry and the condition in which private enterprise should be allowed to operate must be judged in this context.' The industrial field was accordingly divided into three groups: (*a*) strategic industries which should be the exclusive monopoly of the State, e. g. manufacture of arms and ammunition, atomic energy and railway transport, with the proviso that, in an emergency, Government could take over other industries considered vital for national defence; (*b*) key industries like coal, iron and steel, aircraft manufacture, shipbuilding, manufacture of telephone, telegraph and wireless apparatus, and mineral oils, where existing private concerns would be allowed to operate for the next ten years, subject to the inherent right of the State to acquire any of them in the public interest and to the stipulation that the establishment of new undertakings in this field should be the responsibility of the State and other public authorities; and (*c*) remaining indus-

[1] The year 1947 may aptly be called the 'great divide' in the history of India.

tries, where private enterprise would be allowed to operate, subject to such Government control and regulation as were considered necessary. A year after, i.e. in April 1949, Government set up a Fiscal Commission (*a*) to examine working of the policy of the Government of India with regard to the protection of industries since 1922 when the last Fiscal Commission reported and (*b*) to make recommendations as to the future policy which Government should adopt in regard to protection to, and assistance of, industries, and the treatment and obligation of the industries which may be protected and assisted. Finally, it set up, in October 1950, a committee to consider what amendments were necessary in the Indian Companies Act, 1913, as amended in 1936, mainly for the healthy growth of joint-stock enterprises and to adequately safeguard the interests of investors and the general public.

While these commissions and committees got down to work, the Constitution of India was being framed, laying down the 'Directive Principles' of State policy. For the first time it was laid down, in clear and unequivocal language, that the State shall so direct its policy that (*a*) ownership and control of the material resources of the community are distributed to subserve the common good, and (*b*) the operation of the economic system shall not result in the concentration of wealth and means of production to the common detriment.

The Fiscal Commission submitted its report in June 1950 and the Company Law Committee its report in January 1952. Meanwhile, the Planning Commission had got down to business and in its Report dated 7 December 1952, had laid down the objectives, techniques and priorities in planning. Speaking of the backwardness of the Indian economy, the Planning Commission said in 1952 that 'the problem was not merely one of making the existing economic institutions work more efficiently, or making small adjustments in them. What was required was a transformation of that system so as to ensure greater efficiency as well as equality and justice. There were risks in going too far or too fast in these matters, but the risks of not moving fast enough were no less serious.' And again: 'It is clear that, in the transformation of the economy

that is called for, the State will have to play the crucial role. Whether one thinks of the problem of capital formation or of introduction of new techniques or of the extension of social services or of the overall re-alignment of the productive forces and class relationships within society, one comes inevitably to the conclusion that a rapid expansion of the economic and social responsibilities of the State will alone be capable of satisfying the legitimate expectations of the people.'[1]

The Commission also referred specifically to the relative shares of the public and private sectors in the ownership of productive capacity and reiterated the division of the sphere of responsibility laid down in the Industrial Policy Statement of 1948. In regard to the private sector, the Commission bluntly stated that 'private enterprise should have a public purpose.' There was no such thing under modern conditions as completely unregulated and free private enterprise. 'The view that private enterprise should function only on the basis of unregulated profits is an anachronism.' The Commission, however, added that private and public sectors should not be looked upon as two separate entities: they are, and must function as, parts of a single organism.

The issue received a further seal of approval in the Economic Policy Resolution passed by the Avadi session of the Indian National Congress held in January, 1955. Soon after this, Government announced a new Industrial Policy in a Resolution dated April 30, 1956, which stated that, in order to realise the objective of the socialist pattern of society, it was essential to expand the public sector. 'This would provide the economic foundation for increasing opportunities for gainful employment and improving living standards and working conditions for the mass of the people. It would also reduce disparities in income and wealth, prevent private monopoly and the concentration of economic power in the hands of small numbers of individuals. Accordingly, the State must progressively assume a predominant and direct responsibility for setting up new industrial undertakings and for developing transport facilities.'[2]

[1] Planning Commission, *The First Five-Year Plan*, New Delhi, 1952.
[2] Planning Commission, *The Second Five-Year Plan*, New Delhi, 1956.

Nevertheless, Government recognised that there were limiting factors which made it necessary (*a*) to define the field in which the State should undertake *sole* responsibility for further development and (*b*) to make a selection of industries in the development of which it would play at best a *secondary* role. Industries were accordingly classified afresh into three categories. These three categories were (*i*) industries, the further development of which would be the exclusive responsibility of the State, e. g. defence industries, atomic energy, iron and steel, coal and lignite, mineral oils, aircraft, air transport, railway transport, shipbuilding, telephones and telephone cables, telegraphs and wireless apparatus, heavy plant and machinery, generation and distribution of electricity, etc.; (*ii*) industries which would be progressively State-owned, but in which private enterprise could continue to operate, e.g. machine tools, fertilisers, synthetic rubber, road transport, sea transport, ferrous alloy and tools, etc; and (*iii*) all the remaining industries, the further development of which would, in general, be left to the initiative and enterprise of the private sector.

In pursuance of these objectives, very large investments have been, and are being, made by Government in the public sector. In the First Plan period, the actual outlay on large-scale industries and programmes of mineral development in the public sector was only Rs 60 crores, while the estimated outlay by private enterprise was Rs 340 crores. During the Second Plan period, however, new investments in the public sector amounted to Rs 870 crores as against Rs 675 crores in the private sector. The Third Five Year Plan envisages a further stepping up of industrial programmes in the public sector. The present allocation is Rs 1,520 crores.[1]

As a result, the industrial landscape in India today is no longer what it was a quarter of a century or even a decade ago. Rapid development of basic and heavy industries is taking place—in both sectors. While 'industry' proper accounted for 18.5% of the total allocation in the Second Plan,

[1] The outlays of Rs 340 crores and Rs 675 crores respectively in the private sector were inclusive of investments on expansion, replacement and modernisation. Vide also *Appendix* XXXIV.

taken together with transport, communications and power, more than half the Plan expenditure was on basic 'heavy' enterprises. The objective of Government is to raise the proportion of capital goods in the economy and to place the country in the 'take-off' stage of economic growth. Many competent observers agree that this can perhaps be achieved at the end of the Third Five-Year Plan, provided wise policies are pursued and certain extravagantly expensive 'prestige projects' abandoned in favour of schemes which would activise economic incentives.[1]

[1] Daniel L. Spencer, *India—Mixed Enterprise and Western Business*, The Hague 1959. See also Dr. V. Anstey's article, *India's Take-off Problem*, in the 1959-60 Annual Number of *Capital*, Calcutta.

CHAPTER II

THE FINANCING OF INDUSTRIAL ENTERPRISE: PRINCIPLES AND TECHNIQUES

The Principles of Financing Industry

WHEN INDUSTRIES in India were grouped in small villages and towns and in small establishments, and when they catered for limited markets, the problem of financing them was very simple.[1] Capitalist economy and large-scale production, however, brought in their train the formidable problem of finding finance for them: competition on a large scale, which is the keynote of modern capitalistic organisation, demands that an enterprise, in order to be able to hold its own, must be in a position to get the necessary finance smoothly, regularly and easily, and at a reasonable rate.

Far too many conflicting and vague statements regarding the 'financial requirements' of industries in India have been made in recent years. Not infrequently, people have forgotten the fundamental distinction between block or fixed capital and working capital, and have stated that it is the business of banks or the State to find both. On the other hand, it has been asserted by many upholders of the doctrine of 'free enterprise' that the necessary block or fixed capital must come from the general public or at best from 'institutional investors' and that once this is obtained, no well-managed concern need have any difficulty in obtaining the requisite working capital or even capital for extension and replacements.

Let us first analyse the financial requirements of modern industry. In general, industry needs two types of capital, viz. (*a*) fixed or long-term capital for the purchase of block assets such as land, machinery and buildings, and (*b*) working or short-term capital for financing stocks of raw materials, stores and finished products and for meeting day-to-day requirements. In addition, it requires capital for extension and replacement which is usually of a long-term nature, though a part of it may be considered to be medium-term.

[1] N. Das, *Banking and Industrial Finance in India*, Calcutta, 1936.

Even as regards working capital, that part of it which is necessary for holding a minimum level of raw materials, stores and finished goods in an industry is of the nature of permanent capital and only the balance may be treated as short-term capital.

There is, however, no unanimity of opinion regarding the periods for which short-term, medium-term and long-term capital is required by industry. The Committee on State Industrial Finance Corporation in West Bengal, which reported in 1951, regarded short-term credits as those lent for periods up to one year, medium-term credits as those advanced for periods varying from one year to ten years, and long-term credits as those made for periods over ten years. This classification should not, however, be regarded as sacrosanct: it can only serve as working guide.[1]

The relative proportion between block and working capital required in an enterprise varies from industry to industry. As the process of production becomes more and more roundabout or capitalistic, the proportion of fixed to working capital required increases. In such industries as hydro-electric, iron and steel, mining, petroleum refining, and even in jute and cotton, block capital is very large as compared to working capital. On the other hand, in the case of the cottage and small-scale industries, where production is carried on under the simplest conditions and with the most inexpensive tools and implements, the reverse is the case. But it is not improbable that in some such cases, although the proportion of fixed to working capital is not large, the *actual volume* of working capital needed is still very considerable.

The amount of working capital needed in an industry would depend mainly upon the value of the output and the average length of time occupied by the productive process. But there are other governing circumstances as well. The time at which a manufacturer gets paid and the methods of buying raw materials and effecting sales often affect the amount of working capital needed by a particular enterprise of industry.[2]

[1] The Committee on Finance for the Private Sector, popularly known as the Shroff Committee, which reported in April 1954, also tentatively accepted this classification in the absence of anything better or more precise.

[2] P. S. Lokanathan, *Industrial Organisation in India*, London, 1935.

Capital Requirements of Industry

It is very difficult to make an exact estimate of the capital requirements of particular concerns in an industry, because the estimate must of necessity vary with what one considers to be the 'optimum size' of a unit in that industry. Certain figures about average or representative establishments in some of the industries are to be found in the various reports of the Indian Tariff Board, but most of these have become out of date, partly on account of the steep rise in the general price level since 1939 and partly because new machinery and techniques are rapidly replacing old methods of manufacture in almost all branches of industry. Thus, in the cotton mills industry, the introduction of superior types of looms, the automation of looms and the almost complete substitution by machinery of manual methods of bleaching and dyeing in the finishing of processing departments considerably added to fixed capital costs, while superior types of labour deployment also had their repercussions on the ratio of labour to capital equipment.[1] Today, the smallest sugar or cement plant costs Rs 1 crore and a paper factory several crores.

The penetration of science into industry has further changed the pattern of capital requirements. Even in old-established industries, scientific methods are being applied to the choice of materials, techniques of production, control of processes, design of products and specification of standards for products. These require capital expenditure on a vast scale. The result has been that, in India as in other countries, despite the assistance given by the State to small industries, the pendulum is swinging in favour of units which can draw upon, or have access to, virtually unlimited funds.[2]

In an interesting study of capital intensity and use of labour and capital in five major industries in India (cement, paper, iron and steel, cotton textiles and sugar), it has been shown that the trend since 1947 has been towards an absolute

[1] S. D. Mehta, *The Indian Cotton Textile Industry*, Bombay, 1953. Dr. Mehta has also pointed out that, between 1937 and 1951, the financial implications of mill operation grew considerably in dimension, the assets of 50 typical companies surveyed by him having recorded an advance of the order of 175 per cent.

[2] R. S. Edwards and H. Townsend, *Business Enterprise—Its Growth and Organisation*, London, 1958.

increase in gross fixed assets, most of it representing investment in machinery. There has also been a considerable increase in capital-output ratio. All this is the result of (*a*) greater scope for labour-saving machinery and (*b*) the greater access to capital by the larger firms.[1]

The increased requirements of capital by industry, both for starting new units and for expanding and modernising existing ones, have thus accelerated a process in which only the strong can hope to survive. It is true that, under the umbrella of protection (and a virtual stoppage of competing imports), or of a planned reservation of certain sectors for small enterprises, it may become possible for less efficient units to function for some time, but, as every student of economics is aware, such 'protection' cannot be continued indefinitely. In other words, sooner or later, the minimum economic unit, with its minimum requirements of capital, must be accepted as the normal feature. Secondly, even the small industries are no better placed than the big industries in respect of their financial requirements. The quantum of their requirements may be relatively small, but the difficulties they have to encounter are not any less.

Industrial Finance Abroad: Introductory

The question of industrial finance in India and the policy of Government with regard to this particular problem have been so hotly debated in recent years that a proper analysis of the underlying factors at work is impossible without a comparative study of the agencies of industrial finance in countries that are economically more highly developed than India. The study is also important from another point of view. Ever since the days when industrial finance in India presented itself as a problem of some magnitude, people have been loud in their complaint that India has not been following in the footsteps of countries which possessed 'ideal organs of finance' for the promotion and development of their industries. The traditional and conservative ways of banking on the part of the Imperial Bank of India and other joint-stock banks only served to confirm a suspicion that things were manipulated in this country in a certain way by certain

[1] George Rosen, *Industrial Change in India*, Bombay, 1959.

people with interested motives. Until lately, it was openly stated that the State evinced little or no concern for the growth of industrial enterprise, and this lack of enthusiasm was attributed by many to the overwhelming influence which foreign vested interests enjoyed in India and also to the obvious fact that those who governed and directed the industrial policy of the country were not responsible to the representatives of the people for what they did or omitted to do.

Industrial Finance in England

We shall start our study with England, not only because her models have been more or less copied in India but also because her industrial life is decidedly longer and more varied than that of any other country in the world. The first thing that strikes an observer here is that the relations between the British financial world and British industry, as distinguished from British commerce, have never been very close. The proprietors of British banks have invested but a small proportion of their funds in industry and the requirements of the latter have been met more by the 'extremely varied facilities and unrivalled financial machinery of the English capital market' than by the direct participation of banks in industrial ventures.

This peculiarity has been due to historical reasons. In England, commerce preceded industry and London's financial organisation adapted itself to the needs of her commerce. 'The exceptional merits of the City of London lay in the facilities given by the short-term money market for the employment of home or foreign funds; in the financing of trade and commerce, also both home and foreign; and in the issue of foreign bonds, as distinguished from the financing of British industry.' On the other hand, when British industry began its growth in the nineteenth century, there was no particular reason why it should look to the London market for its financial requirements. Industry in those days was, so far as each unit was concerned, on a comparatively small scale; the capital was provided privately and it was built up and extended out of profits; in so far as it required assistance from banks, it found it from the independent banks, often family banks, which in general had their headquarters in the provinces,

and particularly in the Midlands and the North, where the new industries flourished. Moreover, there had existed for many years a large class of investors with means to invest, who exercised an independent judgment as to where to invest, and who did not rely, as in some countries, entirely on their bankers. Although it made full use of the banking facilities offered by the joint-stock banks, industry maintained its independence of any financial control by the latter.

Generally speaking, until very recently, industrial investment in England has not been 'guided' by any financial institution or organisation of any standing or reputation. A few Issue Houses occasionally entered the field of industrial promotion, and the organisations of stockbrokers have often been known to give advice, but banks or other financial institutions hardly fathered an issue or were in any way responsible for it, beyond seeing that the prospectus of a projected company complied generally with the law and that the issue was, on the face of it, respectable. There were practically on established houses to assist the investors in subscribing to shares in local industries and enterprises; the real issuer was 'the company itself, if it was a strong or a good one, or a finance company or syndicate—few large, many small, some good, some indifferent, some bad, and sometimes it was a company or a syndicate got together for the sole purpose of making a particular issue.'[1]

The current requirements of industry were supplied by joint-stock banks. They increased the supply of capital by collecting lodgements from the public; by compounding these lodgements with their own capital and reserve funds, they converted a large number of small quantities and short lengths of capital, individually ineffective, into an aggregate available for productive employment; finally, by a continuous re-distribution of this capital among the points of highest yield, they maximised its earning capacity. This last service of continuous re-distribution of available funds was performed in the City of London by the short-term money market which gave facilities for the employment of home or foreign funds. The money market supplied the day-to-day needs of industry with an elasticity and an efficiency

[1] *Report of the Committee on Finance and Industry*, London, 1931.

that were unknown in any other financial system of the world. On the other hand, intermediate credit (i.e. credit advanced for periods ranging from one or two up to five years) and long-dated capital were not adequately supplied by this market, this being due in part to the historical organisation of British industry and in part to the fact that industry, having grown up on strongly individualistic lines, was anxious to steer clear of anything which might savour of banking control or even interference.

The most important feature of the English credit system was the Bank of England, which stood at the apex of the entire banking organisation of the country. By its control over the cash base of the country, the Bank of England was in a position to regulate the volume of bank deposits, so long as the joint-stock banks adhered to their assets. With the same weapon in its armoury, it could also offset any change which might be made in those practices. The link between the Bank of England and the commercial banks was established through the discount market which was the first outlet of any surplus funds held by the banks and from which funds were withdrawn when they found it necessary to replenish their reserves. If the withdrawal caused a shortage of funds in the market, the market borrowed in some form or other from the Bank of England, and the accommodation thus given by the central institution provided the means of replenishing the cash resources of the commercial banks.

Businessmen in England thus depended on the ordinary credit mechanism of the country for the accommodation they required for purposes of trade and industry. For historical and socio-economic reasons, the system had worked wonderfully well, although the contact between industry and credit had never been very close and intimate. But, with the rise of highly industrialised systems in other countries of Europe and in America, England also found that the old practice of 'little conscious direction of the national activities to definite ends' no longer paid; the feeling grew that her former policy of *laissez-fair* would not ensure her prosperity in a crowded and increasingly competitive world. The question of finding new and up-to-date agencies of industrial finance began to

attract the attention of businessmen and financiers in England as well.

As a direct sequel to the above, there came into existence, during the inter-war period, a number of specialised institutions for providing finance to certain types or groups of industry. Of these, mention may be made of (*a*) the Securities Management Trust, a subsidiary company formed by the Bank of England towards the close of 1929 to assist the process of rationalisation and reconstruction in industry; (*b*) the Bankers' Industrial Development Company, a private company set up in 1930 with the Governor of the Bank of England as Chairman;[1] and (*c*) the Credit for Industry, Ltd., launched in March 1934, mainly to provide capital for plant and other purposes for small and medium-sized business. The three institutions mentioned above played only a limited part in promoting industrial ventures: the gap in the financial machinery for meeting the requirements of small and medium industries could not be fully bridged by them.[2]

Two new institutions were accordingly set up in the post-World War II period. The first of these was the Industrial and Commercial Finance Corporation formed in 1945 when the war was drawing to its close. The object was to provide medium-term finance or long-term capital for the smaller and medium-sized industrial or commercial business, where the amounts involved (ranging between £5,000 and £200,000) would not justify, or even possibly permit, the making of a public issue of capital.

The second institution was the Finance Corporation for Industry, Ltd., also set up in 1945, 'to assist the quick rehabilitation and development, in the national interest, of large industries—those not covered by the Industrial and Commercial finance Corporation'.[3] It resembles the Bankers'

[1] The Bankers' Industrial Development Company was characterised by many as 'a national consortium of British bankers—a partnership between the Bank of England and the leading houses of the City of London, formed to make available for British industry the amplest resources of the nation.'

[2] For details, see S. K. Basu, *Industrial Finance in India*, Calcutta, 1956.

[3] The Finance Corporation for Industry Ltd., is wholly owned by a consortium of insurance companies, trust companies and the Bank of England in the proportion of 40, 30 and 30 per cent respectively. The authorised capital is £25 million, but its paid up capital is much less. The bulk of its resources is provided by the exercise of its borrowing powers amounting to four times the authorised capital, i.e. £100 million.

Industrial Development Company in the sense that it takes no initiative in the reorganisation of industry and its primary objective is to provide finance. But it is really a much more ambitious version of the latter in that the emphasis has been shifted from salvage to development. 'It will seek out its own spheres of activity and not wait till the corpses are brought in.' Secondly, it has not been debarred, in the process of financing, from participating in the equity of the business it assists: it can, if it so chooses, subscribe to the initial share capital of such business.[1]

These financial institutions assist in the main *existing* business. They do not, however, completely eschew new firms, if the latter show promise. The I.C.F.C., for instance, has helped enterprises where the promoters have been able to put up a reasonable part of the capital required, but it has consistently declined to advance money to new undertakings which do not satisfy this criterion.[2]

Another special institution was set up in 1953. This is the Commonwealth Development Finance Company, Ltd., established as a channel for the investment of private capital in Commonwealth development schemes. Its issued capital is £26 million, held by the Bank of England and 149 business concerns in the United Kingdom and in other Commonwealth countries. The company is empowered to borrow up to twice its issued capital. At the end of March 1959, its commitments totalled £15.5 million only.

Industrial Finance in Germany

We may now return to a study of the relationship between banks and industry in Germany.[3] A very large section of Indians desire that India should take a leaf out of German industrial history and develop her industries after the German fashion. Even apart from this consideration, the study is important because, of all the Continental countries, Germany shows *par excellence* how economic circumstances forced bankers to associate themselves with industrial development, and how

[1] R. S. Edwards and H. Townsend, *Business Enterprise—Its Growth and Organisation*, London, 1958.
[2] Norman Macrae, *The London Capital Market*, London, 1955.
[3] A very comprehensive account will be found in P. B. Whale, *Joint-Stock Banking in Germany*, London, 1946.

industries themselves were forced to count on the support and guidance of banks.

Let us first analyse the historical forces at work. The close association between banks and industry in Germany arose out of the necessities of the situation—from the scarcity of capital and of independent investors. 'The comparative poverty of Germany about the middle of the last century and the great demand for capital to supply the needs of her rapidly growing industries led naturally to the development of banks which took a large and active part in providing the capital requisite for the creation and extension of business undertakings, both by the grant of long loans and by the floatation of joint-stock companies. In order to compete with England, which had the advantage of an early start, industry in Germany had to turn to banks for its capital requirements. Accepting the heavy responsibility of supplying capital to industry, banks on their part were compelled to keep in more intimate touch with, and maintain a more continuous watch over, firms with which they had allied themselves than were the English banks.'[1]

It was not exactly an *absolute* shortage of capital that resulted in this peculiar relationship between German banks and industry. Capital there was, but it was misdirected. 'Those who had the necessary funds were for the most part neither willing nor fitted to become progressive entrepreneurs themselves, nor would they entrust their money to others who had the required qualities.' Hence there was an urgent need for some agency which could obtain the confidence of the investing classes and use this confidence to direct the capital towards sound industrial undertakings. The new credit banks filled this gap.

The close co-operation between banks and industry in Germany was accelerated by some of the outstanding features of industrial and economic life there. During the closing years of the last century, kartellization, or the association of industries horizontally related, began to dominate the economic landscape in Germany: industry became powerfully equipped through efficient organization to meet competition abroad and to secure a stable and remunerative price in

[1] *Report of the Committee on Finance and Industry*, London, 1931, pp. 162-3.

the home market. 'But large and highly organized industrial interests called for large and similarly efficient industrial finance. The advantages which industrial groups had gained by close co-operation under the kartel system were realized by the banking interests, which not only began to form syndicates or consortiums among themselves in order to distribute the risks and burdens of large-scale finance, but also began to demand representation on the advisory councils of the concerns or groups which they financed.'[1] By the beginning of the twentieth century, the greater banks had their recognized industrial areas, so to speak. The economic expansion had created, on the one hand, such heavy demands for credits of all descriptions, and claimed, on the other hand, the public trust in such a measure that, broadly speaking, the means and position of private houses were no longer equal to the requirements. The process of concentration and affiliation in industry necessitated the broadening of the capital and credit basis of the banks themselves, and this latter process in its turn enabled the banks to form a close alliance with industrial concerns.[2]

What is often overlooked in all discussions about the German banking system is that the special services to industry were performed not by a separate or special type of credit agency, but by the ordinary joint-stock or commercial banks. The various activities carried out in the British banking system by various kinds of agencies were executed in Germany by the joint-stock banks alone: these latter comprised the functions of a commercial bank, mortgage bank, discount house, issue house, company promoter, bill-broker, and stock-broker, 'The German Great Bank, unlike the English Investment Trust, did not specialize in investment business alone, but combined the functions of an investment bank with those of an ordinary commercial bank.' The ordinary credit banks carried on various lines of business which to an outsider would seem rather risky and speculative. But, inside the integrated system, there was a considerable amount of specialization. The various routine transactions were done by the respective departments, while the higher financial activities, such as the floating of

[1] *The Bankers' Magazine*, London, April 1931.
[2] Leopold Joseph, *The Evolution of German Banking*, London, 1931.

State and municipal loans, syndicate operations in connexion with the promotion of industrial undertakings, etc. were dealt with by the managing directors themselves with the help of their secretaries.[1] Organization, elaborate and methodical, characterized the German system and gave it power. In banking, as in industry, though the individual units were often large enough by themselves, the method of the kartel was frequently adopted. On the one hand, each of the leading banks had a large group of allied banks, working in general co-operation with it; on the other, in addition to this primary grouping, they were specially organized in their own ways to deal with large financial propositions. The result was that, in Germany, risks which even the largest banks might regard as dangerous were made quite manageable by distribution.[2]

Let us now analyse the transactions which took place between a bank and a particular customer undertaking. These transactions were very varied—a sort of 'an indivisible many-sided whole, rather than a sum of separate relations.' The first connexion arose in the matter of current account which was distinct from cheque account. When a current account relationship existed between the two parties, money claims arose on both sides and 'these claims were not settled individually, but were treated as items in an account of which the balance was struck periodically.' The average German firm depended to a remarkable extent on this arrangement not only for its working funds but also for the purpose of extending its permanent assets in anticipation of recourse to the investment market. The current account relationship was very important, as it was a continuous connexion and thus gave the bank an insight into most of the money transactions of a customer; it also provided much of the data required for estimating the risk involved in the intermittent capital transactions: and it led up to capital transactions even more directly, in the sense that improvements and extensions of plant were often undertaken by means of current account credit which was repaid later with the proceeds of a capital issue. The industrial current account was the pivot

[1] *Written Evidence of Dr. L. Nemenyi before the Indian Central Banking Committee*, 1931, Vol. II.

[2] H. S. Foxwell, *Papers on Current Finance*, London, 1932.

of all transactions between banks and industry; promotion and issue transactions, direct participation in industrial undertakings and co-operation in management through Boards of Supervisors—these stood in very many cases in a close causal sequence with bank credit.[1]

The second important connexion arose in the matter of promoting companies and equipping them with capital. The more common method of promotion in Germany was what was called 'the simultaneous method' whereby the entire capital was taken over in the first instance by the promoters themselves. What happened was this. After the plans of a new company had been examined and approved by a bank, a so-called 'syndicate' (a sort of temporary association of various banks and also of private men for the sake of floating a new concern) was formed, and the shares of the new company were taken up by the promoters, that is, the members of the syndicate. This, however, was only the first step. For the satisfactory termination of the whole transaction, the shares taken over at the time of promotion had to be placed before the investing public. This also was done by the syndicate or consortium. The time was always chosen carefully, according to the conditions of the share market. The syndicate divided the shares between the applicants, but the period of sale was always regulated in such a manner that the shares could be sold at the highest price obtainable. In all this, banks played the part of middlemen only: they simply held the securities for a certain length of time, and lasting participation in industrial undertakings was never their general policy.[2]

The third and last important connexion arose in the representation accorded to banks on the Board of Supervisors of an industrial undertaking. This Board came in between the Executive and the General Meeting of shareholders to keep a check on the executive in the interests of shareholders and had got considerable powers over both. By this means banks strengthened their connexion with the undertakings in question and exercised more influence on their policy and more insight into its execution.

[1] P. B. Whale, *Joint-stock Banking in Germany*, London, 1946.
[2] *ibid.*

It may be asked how German banks managed to maintain such a close alliance with industry without involving themselves in trouble. The secret was that every line of the activities of a German credit bank was self-balancing. 'The short-term deposits were used only for short-term credit, whereas the loans on long terms were based, without exception, on such resources as could be safely locked up for long periods. The latter were granted to industry and agriculture in the form of debentures, and the debenture bonds which were issued against these loans were again sold to capitalists who were willing to invest their money for a long period against a guaranteed interest.' The German banks did not unduly 'lock up' their assets: they could take an active share in industrial banking simply because they had vast resources of their own and large reserves.[1] Although it is true that German banks invested in the shares of their customers' concerns, it is not true, contrary to the general opinion held in India, that they tied up their depositors' funds to any appreciable extent in illiquid assets. The total of illiquid assets was almost invariably covered by the capital and reserve resources of a bank. Then again, even when a certain amount of 'locking up' became unavoidable, the risks were mitigated, firstly, by diversifying their interests and, secondly, by maintaining secret reserves. Thus, in syndicate operations, the capital invested was constantly changed from one investment to another, and the holdings of banks in the different syndicates were kept very confidential.[2]

A Comparison of the English and German Systems and Some Recent Developments

The English banking system was an instance of excessive division of labour, but it suited the temperament of the English people and had historical forces behind it. In Germany, banking was more non-specialized, and it was almost a marvel that ordinary commercial banks should engage in activities of so diverse and complex a character and yet

[1] Reisser tells us, as the result of an enquiry into 169 banks, that the paid-up capital and reserves of these banks was 45 per cent of their liabilities, while the proportion in England at that time was only 9 per cent.

[2] *Written Evidence of Dr. L. Nemenyi before the Indian Central Banking Enquiry Committee*, 1931, Vol. II.

maintain their soundness and liquidity. As we have seen already, this was achieved by a punctilious insistence on self-balancing transactions and by a judicious distribution of risks. The German system provided a very efficient machinery for investigating business ventures and at the same time was strong enough to sustain the heavy risks to which industry is exposed. The companies enjoyed expert financial advice and assistance; the banks, by virtue of their position as directing heads of industrial groups, obtained a comprehensive view of economic conditions which enabled them to promote amalgamations and introduce or, if necessary, even force through schemes of rationalization or other remedial measures. The investing public also benefited inasmuch as it obtained as a matter of course a large measure of security through the active intervention of banks. Moreover, as the German banker undertook a more definite responsibility and a greater risk in connexion with capital issues, he was naturally more concerned about the success and stability of the securities issued under his name than the average English banker.

On the other hand, certain weak features of the German system should not be overlooked. While the charge of having caused the annihilation of small business in Germany should not be laid at the door of the credit banks, it cannot be denied that one of the far-reaching results of the direct intermingling of the vital interests of the banks and of industry has been that the value of the small capitalist and investor has been somewhat over-looked, and the State has often been forced to step in to avert a crisis.[1] Moreover, in the years before World War I, the ordinary industrial or commercial firm of moderate means often found its freedom of action conditioned by the goodwill of its bank, even when it was in a sound and fairly prosperous state itself. Although initiation in industrial combination did not actually come from the banks, it is difficult to dispute the fact that banks had some part in the development. At a very early stage they helped to prepare the way by encouraging fusions between individual undertakings, and thus reducing the number of competitors. Throughout, their attitude towards fusions was sympathetic, even while it remained passive. Finally, once the plans for combination had reached a certain

[1] *The Bankers' Magazine*, London, April 1932.

stage and were within a measurable distance of fruition, the banks gave active support to ensure their success.[1]

Another weakness of the German system lay in the relation of banks to the short-term money market. In their desire to meet the credit needs of their industrial customers on the cheapest terms, the banks placed their acceptances at the disposal of their customers to a very large extent. Such acceptances were used largely to obtain long-term credits. Now, a demand for long-term credit for capital investment means more bank acceptances and a tendency towards over-burdening of the money market, with the result that the interest rate of legitimate short-term credit reflected in the discount rate is forced up without justification and at a time when trade expansion may be vitally necessary. The practice of the banks employing the nation's liquid resources as long-term advances to industry had a disturbing influence on the money market on more occasions than one and, paradoxical though it may seem, the rapid reconstruction of Germany's industrial plant after World War I with the active help of banks was, through its effect on the money market, a major obstacle to the desired expansion of the country's foreign trade.[2]

In spite of these weaknesses, the system was undoubtedly suited to the genius of the German people, and a signal success in so far as the industrial development of the country was concerned. The banks assisted with their credit in the development of production on a large scale and their decentralization of establishments, combined with an elaborate and methodical organization, had enabled them to keep a finger 'on everything that was going on'. Finance and industry had gone hand in hand and the grim determination of the German people to achieve a rapid economic development had only strengthened this process of alliance. The influence of the old bureaucracy also was not negligible: it was this bureaucracy that ensured economic stability by restricting the liberty of the industrial unit and thus built up a banking tradition which lost none of its essential characteristics during the difficult inflation years.[3]

[1] J. H. Clapham, *The Economic Development of France and Germany*, Cambridge, 1938.
[2] J. W. Angell, *The Recovery of Germany*, New Haven, 1939.
[3] *The Bankers' Magazine*, London, June 1930.

Developments in Germany during the inter-war period, however, revealed certain weaknesses in this relationship between banks and industry. War profits increased the power and independence of industry as against banks, and banks were seriously affected by the fall in the value of the mark.[1] Although stabilization came after some time, banks could not go back to their strong pre-World War I position. As a matter of fact, the balance sheets of the leading German banks, while showing substantial expansion in resources, seemed to bear a greater resemblance to the normal English balance sheet than did the majority of the German balance sheets in pre-war days. Moreover, the melancholy bank failures that took place in Austria and Germany in 1930 and after, showed far too clearly that the system of mixed industrial banking had helped to make Germany's economy more vulnerable. Germany's economic depression of 1932-3 was certainly aggravated, and her financial crisis caused, by the destruction of her working capital during the inflation period and by the sudden withdrawal of foreign confidence and money, but there is not a shadow of doubt that her system of intimate alliance of banks with industry had made her position inherently weak.[2] So when the crisis came, nothing could lessen the steepness of the crash.

One of the most striking features of German banking legislation during the inter-war period was the separation of commercial from investment banking. Following the crisis of 1931 and the complete breakdown of the German banking system, a Commission of Investigation was set up in 1934 and, later, a new law, the German Credit Act of 5 December 1934, was passed. Under this Act, banks were called upon to maintain a fairly high standard of liquidity and to limit their holdings of real estate and speculative investments. Permanent participation and investment in property and buildings were not to exceed the capital and reserves of the credit institution concerned, As a result, syndicate participation by the five big Berlin banks declined from 168 million Reichsmarks in 1929 to only 83 million Reichsmarks in 1939.

[1] H. Schacht, *The End of Reparations,* translated by Lewis Gannett, London, 1931.

[2] Dr. Erich Roll in *The Bankers' Magazine,* London, February 1933.

Another interesting development in Germany during the inter-war period was the financing of industry largely out of undistributed profits. According to one estimate, during the decade ending in 1942, nearly 10,000 million Reichsmarks out of a total of 14,000 million Reichsmarks required by industry was found by the ploughing back of profits. Business credits by banks declined from about 40 per cent of the total balance sheet in 1938 to about 20 per cent in 1942.

At the end of World War II and after the currency and credit reform of 1948, banks in West Germany had to provide extensive medium-term credit for the restoration of mills and factories devastated by the war. While no exact figures are available of how much has been tied up in medium - and how much in long-term credits, the situation is well under control, as the Bank Deutscher Laendar has extensive regulating powers over all banks. Re-discount facilities which had played such a vital part in financing German industry before the war, have also regained much of their importance as a method of restoring bank liquidity. As a result, larger companies in particular have been able to obtain from the banks much 'intermediate' finance, on a revolving basis, and until enough profits could be earned to pay back the money borrowed. By taking care also of the working capital requirements of their industrial customers—large and small—the deposit banks have made it easier for them to use their retained profits for additions to the capital equipment.[1]

A significant development in the post-World-War II period has been the re-constitution, in 1949, of a private institution specialising in long-term loans to industry. This is the Industries Kredit Bank, A. G., in Düsseldorf, formed to take over and continue the business of the old Bank für Deutsche Industrie-obligation. The I. K. B. does not receive deposits from the public and its loans are mostly on a secured basis. It draws its resources from (*a*) issues of bearer-bonds, (*b*) loans from public institutions, partly 'counter-part funds' of the Marshall aid, and (*c*) its own share-capital. According to a Report prepared by the O.E.E.C., the I.K.B. has been working

[1] Organisation for European Economic Co-operation, *The Supply of Capital Funds for Industrial Development in Europe*, Paris, 1957. See also article entitled 'Banks' Big Stake in the Growth of Industry in Germany' by Dr. Hanns Deuss in the *Financial Times*, London, March 28, 1960.

with remarkable success, in spite of great difficulties in raising funds on the capital market.

Another institution for long-term lending is the Kreditanstalt für Wiederaufbahn (K.F.W.), a public corporation established at Frankfurt a.M. in 1948. Its capital is only 1 million D. M. held by the Federal and Laendar Governments, but various reserves have accumulated to the extent of 190 million D.M. The K.F.W. has helped both large companies and public utilities, particularly the railways.

It may be noted, however, that, as in the U.K., the real difficulty has been not any lack of finance, but lack of incentive to expand business activity under conditions of crippling taxation. Industry began to look up only from 1954 onwards when the corporate plus trade tax was brought down to 55%. The new economic policy launched by Dr. Ludwig Erhard also helped.[1]

In England, too, the trend has been towards a much closer association between banks and industry, The Big Five in the English banking system have now got considerable investment in industrial shares and debentures, and although they are still unwilling to be drawn into too intimate a relationship with industry, the connections which the inter-war years brought about, have endured. 'The problem today does bot seem to lie in the lack of appropriate financial institutions: it lies instead in the level of tax rates on business profits.'

Mixed Banking in India on the German Model

It has been suggested by many that Indian joint-stock banks should pursue a policy of mixed banking, i.e. combine investment banking with commercial banking, on the lines followed by German banks before 1934. Now, few of the joint-stock banks in this country are fitted to embark on the undoubtedly difficult and complex policy of mixed banking. This is for a variety of reasons. Firstly, although the size of the scheduled banks has increased during the last two decades, they are still small when compared with their Continental counterparts. Secondly, their deposit assets which consist largely of customers' deposits liable to be withdrawn at short notice, cannot

[1] Ludwig Erhard, *Prosperity through Competition*, London, 1958.

obviously, without incurring serious risks, be locked up in long-term loans or advances to industry. Thirdly, the necessary technical and entrepreneurial ability, which is required if mixed banking policy is to be successful, is still lacking among our bankers. The large number of bank failures which have occurred from time to time since 1913 do not offer much hope for this type of banking. The whole history of industrial finance in India shows that investment banking by institutions which are organised as commercial banks inevitably leads to speculation and rash promotion. The remarks made by a German banking expert (Dr. O. Jeidels) before the Indian Central Banking Enquiry Committee thirty years ago, hold good even today. 'It is not to the advantage either of the commercial banking system or Indian industries that any of the weaker banks should participate in industrial financing. This new class of business requires much experience and an established policy of sound banking. It also demands considerable capital and a firm resistance to speculative temptations which easily arise in a line of business where securities are created and sold. The bulk of the joint-stock banks in India are at present not ready for this activity, and even the larger ones can cultivate it only slowly, with great caution, and preferably under competent guidance as participants in strong syndicates.'

Another point that is important for India to remember is that in Germany block capital was hardly, if ever, provided by banks. Their share and syndicate operations were in the nature of guarantees only: they did not supply the initial block capital themselves. As regards the success of the current account system in Germany, it should not be forgotten that this was due ultimately to the fact that the savings of the community there (which are the ultimate source of capital) were poured into those credit banks in enormous quantities for years together.[1]

What was needed in India, therefore, was not so much mixed banking on the German model, but the setting up of special institutions to cater for the requirements of various types of industry. Government had already taken note of

[1] Solomon Flink, *The German Reichsbank and Economic Germany*, New York, 1936.

the 'gap' which existed in the country and had set up, within the past few years, quite a number of such institutions. We shall study the working of these institutions in a subsequent chapter.

CHAPTER III

THE FINANCING OF INDUSTRIAL ENTERPRISE IN INDIA : YESTERDAY AND TODAY

Introductory

THE PROBLEM of providing necessary finance for industrial development in any country has two aspects. Firstly, there is the macroeconomic aspect of aggregate savings and demand for investment and the factors that bear on the generation of savings and formation of capital. Secondly, there is the role of different institutions and agencies that function as intermediaries in channelling savings to the units in need of funds. While the two aspects cannot be wholly separated from each other, we shall confine ourselves in this chapter to the second aspect only.

How Fixed Capital is Raised for Industry in India

So far, most of the major industries in India have obtained their fixed capital either by public or private subscription of shares or debentures of the undertaking, or by direct deposits, or by the system of providing money on private account by an individual or partnership. The part played by these diverse methods has of course varied from industry to industry, but the recent tendency has been towards securing the initial block of fixed capital by public or private subscription of shares or debentures.

Although the market for equities had considerably broadened since 1939, even a decade ago it was the experience of industries in general that it was more difficult to raise such capital in India than in the industrialised countries of the West.[1] The figures of paid-up capital of joint-stock companies in India in those years showed that, notwithstanding the launching of a number of new undertakings involving fairly large capital, the *average* paid-up capital of joint-stock companies in India had not registered any significant increase.

Some idea of the sluggish conditions obtaining in the capital market in those years can be had from the figures of

[1] *Report of the Committee on Finance for the Private Sector*, Bombay, 1954.

consents granted for new issues by the Controller of Capital Issues under the Capital Issues (Continuance of Control) Act, 1947, and of the actual amounts raised by such companies as had furnished the relevant returns. They showed that the amount of capital sanctioned bore little relation to the actual amount of capital raised. Taking an average of the seven years 1948-54, the annual amount sanctioned (i.e. industrial issues consented to) was Rs 60 crores, whereas the amount of capital actually raised was an average of only Rs 18.5 crores per annum.[1]

As soon as the First Five Year Plan got into stride, however, a distinct change could be noticed in the mood of entrepreneurs and investors. As the Second Plan began to run its course more or less smoothly, thanks to the assistance India received from the U.S.A., U.K., U.S.S.R., West Germany and the various international agencies for financing development, the Indian capital market underwent a complete metamorphosis. There was a hectic boom on the stock exchange, easy-money conditions became more or less general all over the country, and appeals to the investing public began to be issued almost at a torrential rate. Some of these were for new floatations, while, in other cases, existing companies came into the investment market with new issues of share capital. During 1959 and 1960, many of the new capital issues, particularly those involving foreign collaboration, were heavily oversubscribed. Transactions took place even before shares were finally allotted by the companies in response to applications. Some of these deals took place at fantastic prices. One possible reason for this was perhaps the hunger for 'growth potential' investments, forced by high taxes on income and inflationary trends. Whatever the reason, there was no longer any difficulty on the part of any reasonably good company in raising the requisite capital from the open market.[2]

It may be noted in this connexion that most of the paid-up capital of joint-stock companies in India is ordinary or common

[1] Vide Annual Reports on *The Working of Capital Issues Control* issued by the Government of India, Department of Company Law Administration.

[2] The Committee on Finance for the Private Sector, which reported in 1954, would have had a very different story to tell if it had been set up only five years later.

stock. Preference shares have been issued in some cases, but they have not been very popular in India. According to a study made by a Calcutta economist, the only industry which has made any substantial use of the device of preference shares is the jute industry and the Tata Iron & Steel Co., Ltd.[1] It appears that both preference and deferred shares are popular mainly in such undertakings as have a well-established record of activity and whose future prospects also appear to be fairly bright to the general body of investors.

Unlike in Western countries, debenture finance has not played an important part in meeting the fixed capital requirements of industry in India. In Europe, extensions and replacements, or even normal working expenses, are generally met by the issue of debentures. In India, on the other hand, debentures form a very small proportion of the total capital of industrial undertakings. According to a study made by the Indian Central Banking Enquiry Committee in 1931, the debenture floatation was insignificant, as would be evident from the following figures:

		Joint-stock companies on the Calcutta list	*Joint-stock companies on the Bombay list*
Share Capital	..	Rs 76.30 crores	Rs 52.83 crores
Debentures	..	Rs 8.65 ,,	Rs 17.51 ,,

The position has not altered substantially since. Out of 50 cotton mills quoted in the *Investors' India Year Book*, 1960, only 18 had issued debenture capital, but the percentage of debentures to the total capital had increased from 1.2 in 1955 to 5.5 in 1959. On the other hand, the proportion of debebtures to share capital had gone down in the jute, tea and coal industries. There had, however, been a substantial increase in the sugar and engineering industries.[2]

In the inter-war period, both preference shares and debentures became extremely popular with investors in European countries and the U.S.A. This was because the average investor wanted to have a fixed return on his money rather than a share in the full risks of the industry. The tendency was also

[1] S. K. Basu, *Industrial Finance in India, Calcutta*, 1956.

[2] Of late, there has been a slight increase in debenture issues, but the proportion of *new* debenture issues to *new* issues of ordinary shares remains more or less the same. See also Chapter XII.

partly the result of an increase in the amounts of capital accumulated by financial institutions such as insurance companies: these latter naturally preferred their industrial investments to be in the form of preference shares and debentures rather than ordinary or deferred shares.

The reasons for the unpopularity of debentures in this country are many and sometimes contradictory. According to some witnesses who deposed before the Indian Central Banking Enquiry Committee in 1931, debentures were not a popular method of investment with Indians, because speculation had an attraction for most Indian investors. The main consideration with them was capital appreciation rather than a steady yield, and debentures offered little scope in the former direction. But this does not offer a satisfactory explanation. It is well known that every year large sums of money are invested in fixed interest-bearing Government securities, postal cash certificates, national savings certificates and municipal and port trust loans. If speculation were the prime consideration, why should Indian investors put such large sums of money in Government and quasi-Government bonds?

The real reason for the comparatively limited use made of debentures as an instrument for attracting capital appears to be that debentures suffer from a double disadvantage. If a fixed return is the primary consideration, the investor would naturally prefer to put his money in Government and quasi-Government bonds rather than in industrial bonds or debentures, for, after all, the former are much safer than the latter. Barring one or two companies like the Tata Iron & Steel Co., Ltd., debentures, wherever issued, were taken up by former Indian princes or by wealthy merchants. Unlike in Western countries, debenture issue has never been broad-based in our country.

A further explanation of the relative unpopularity of debentures can be found in the attitude of commercial banks in India. For reasons which are not quite clear, industrial concerns which have issued debentures have not been looked upon with favour by joint-stock banks. According to the Central Banking Enquiry Committee, industrial concerns which had issued debentures found it difficult to secure bank

loans and cash credits on the usual terms. Perhaps some of these banks thought that it was not safe to lend money to an undertaking which already had such heavy debt charges.

Nevertheless, as stated already, the difficulties of obtaining initial capital for industrial ventures no longer exist. During the past ten years or so, industries floated on sound lines and having reasonable prospects of success have not experienced any difficulty in securing financial support from the investing public. This view has been expressed at successive intervals before various Committees and Commissions by the various Chambers of Commerce, the Exchange Banks Association and the Indian Banks Association. The Fiscal Commission which reported in 1950 also remarked on the fact that many of the witnesses laid greater stress on 'other factors' inhibiting industrial enterprise in India rather than on the lack of capital.[1]

Even in the recent past, it was only new industries which sometimes failed to secure adequate support from the investing public. But this is true not merely of India but also of other countries. A special handicap in India was the stepmotherly attitude of Government until 1947, i.e. until India attained her independence. As long as the economic and fiscal policies of Government were guided by extra-national considerations, it was not reasonable to expect the investor to take kindly to every new issue, howsoever attractive it might look on paper. In view of past history, the investor could never be sure of Government's intentions in the matter of industrial development and he could not be blamed if, at times, he wanted to look a bit more carefully before he leapt.[2]

The problems of long-term finance are not, however, confined to the raising of initial capital by means of floatation. As has been stated already, an industrial undertaking requires fairly long-term financial accommodation during the period of development of its business and it is in this sphere that industries sometimes experience difficulties. The amount of capital realised by the sale of shares is soon exhausted in acquiring the land, setting up the factory,

[1] *Report of the Indian Fiscal Commission*, Vol. I, New Delhi, 1950, pp. 175-80.
[2] The Hon'ble Mr. R. K. Shanmukham Chetty expressed a similar view in the Indian Legislative Assembly in November 1947, while speaking on the Industrial Finance Corporation of India Bill.

installing the machinery and providing other facilities to get the concern going. The concern is then faced with the problem of finding the requisite funds to develop and carry on the business. In many industries, several years may have to elapse before an undertaking can reach the stage of earning profits, and it is during this 'period of gestation' that it may find that it cannot have any long or medium-term credit on easy terms.[1]

The above difficulties were often due to the fact that many undertakings were under-capitalised from the very start. Not infrequently, a few promoters or entrepreneurs would commence business with the barest minimum of capital and would make no provision for unforeseen (but sometimes very common) items of expenditure. During the inter-war period, when money was relatively plentiful, a number of new industrial enterprises were started in the country, mainly because the 'climate of investment' appeared favourable. As soon as a slump appeared, these undertakings found that they could not get the additional long-term or medium-term finance to carry on their business . The result was that many of them had to go into liquidation before they could even commence production.[2]

The difficulty of finance became particularly evident in relation to the problem of rationalisation in some of the industries in India. Plant and machinery in some of the older industries in India (e.g. cotton, jute, iron and steel, and collieries) had become archaic and out of date and, therefore, badly required replacement and modernisation. The introduction of new techniques and labour-saving devices in industries in other countries also placed Indian undertakings at a considerable disadvantage and made it imperative that money should be found for rationalisation. Unfortunately, however, many desirable programmes of rationalisation could not be carried out for a long time, partly because the requisite funds were not available.[3]

[1] For details, see S. K. Basu, *Industrial Finance in India*, Calcutta, 1956.

[2] The Annual Reports of the Registrars of Joint-stock Companies are replete with instances of this kind.

[3] Another obstacle in the way of rationalisation is the hostile attitude of labour which resists it on the ground that it would lead to the displacement of labour.

How Working Capital is Found for Industry in India

Coming now to the question of working capital, one is surprised at the variety of ways in which this has been found by different enterprises and industries in India. Broadly speaking, there are four sources of getting working capital—(1) public deposits; (2) private deposits or money on private account provided by one or more of the entrepreneurs, their friends, or the managing agents; (3) advances by indigenous shroffs; (4) advances by joint-stock banks. We shall consider the part played by each of them in the financing of the short and medium-term requirements of industry in India.

(1) *Public Deposits*

We may start with the public deposits.[1] This system prevailed almost solely in the cotton textile industry of Bombay and Ahmedabad—particularly in the latter. The system arose owing to the imperfect banking development of the country: on the one hand, people naturally had more confidence in, and preferred to entrust their savings to, those men in their communities whom they knew and with whom they could deal without the formalities necessary in dealing with banks; on the other, the mill-owners of Bombay and Ahmedabad were ready to accord to depositors a safe return with certain other advantages which the latter could not possibly get from banks run on western lines or from indigenous shroffs. So arose an arrangement whereby the mills got—in the days prior to World War II—most of the working capital from the public on short-term deposits, usually for six months or a year. The importance of this system in the thirties of the present century is illustrated by the following figures.[2]

	Bombay (Figures for 64 mills)		Ahmedabad (Figures for 56 mills)	
	Lakhs of rupees	*Percentage of total finance*	*Lakhs of rupees*	*Percentage of total finance*
1. Amount loaned by the Managing Agents	532	21	264	24
2. Amount loaned by banks ..	226	9	42	4
3. Amount of public deposits ..	273	11	426	39
4. Amount of share capital ..	1,214	49	340	32
5. Amount of debentures ..	238	10	8	1

[1] These 'public deposits' provided both fixed and working capital, but separate figures as to the extent to which they provide these two items are not available.

[2] *Indian Central Banking Enquiry Committee, Minority Report*, 1931. The figures relate to October 1930.

It will be seen from the above that, during the thirties, public deposits were the most important source of industrial finance for the cotton textile industry in Ahmedabad, and they were in excess even of the amount raised through share capital and debentures. In Bombay, the importance of public deposits was much less, but until 1921 (when public confidence in the Bombay cotton mills was rudely shaken), public deposits played as important a part there as they did in Ahmedabad.[1]

Since 1930, however, there has been a substantial decline in the volume of public deposits, particularly in Bombay. In Bombay, public deposits fell from an average of Rs 4.3 lakhs per mill in 1930 to Rs 2 lakhs per mill in 1937, while in Bombay and Ahmedabad taken together, public deposits fell from Rs 12 lakhs per mill in 1935 to Rs 7.5 lakhs per mill in 1939.[2]

This tendency gathered strength during the years following the declaration of World War II, with this difference that very soon managing agents were supplying the finance, enabling themselves to redeem, more or less completely, their own commitments, and to reduce the volume of deposits. This is also indirectly confirmed by the rate of expansion in, and the volume of bank finance available to, cotton mills in Bombay and Ahmedabad from 1930 onwards. There was a ten to fifteen-fold rise in the utilization of normal banking facilities between 1930 and 1958. The stake of banks in the mill industry rose not only in terms of volume, but also in terms of its proportional significance.[3]

The public deposit system of finance has played a very important part in the development of the Indian cotton textile industry. At a time when banking facilities were inadequate, these deposits were a virtual godsend to most cotton mills in Bombay and Ahmedabad. The rates of interest paid on the deposits have never been exorbitant and have generally varied from $4\frac{1}{2}$ to $6\frac{1}{2}$ per cent. In no case were these rates more than 1 per cent above the rate at which loans were advanced by banks and not infrequently they

[1] *Indian Central Banking Enquiry Committee Report*, 1931, Vol. III.
[2] S. D. Mehta, *The Indian Cotton Textile Industry*, Bombay, 1953.
[3] *Reserve Bank of India Bulletin*, April, 1958.

have been even $\frac{1}{2}$ per cent less. Looked at from the interest rate point of view, therefore, these public deposits were never 'costly'. Instead, they were a real convenience to the cotton mills of Bombay and Ahmedabad inasmuch as they enabled the mills to keep their interest charges low and to borrow at cheap rates to pay higher dividends—a feat which would not have been possible if the whole of the working capital had to be raised by other methods. On the other hand, this system of industrial finance had some inherent weaknesses, which were demonstrated during the depression of 1925-30. In times of stringency, it was those mills whose financial position was not very strong which found real difficulty in obtaining deposits, although it was these very mills which needed help: the tendency of depositors to withdraw their money on the slightest rumours of difficult times ahead invariably put the mills in an awkward position. That is precisely what happened in Bombay and, to some extent, in Ahmedabad during 1925-26 and the four years thereafter. Public confidence was shaken and depositors were anxious to withdraw their deposits from all mills—good, bad and indifferent. Some mills had to close down and others had to borrow money from friends and indigenous bankers at high rates of interest. The depositors could not of course be blamed for the way in which they had behaved. They could not possibly follow the movements of the money market and understand what was happening; they were in the position of unsecured creditors, and as there was no intervening banking institution between the mills and themselves, they were apt to be easily led away by any bazaar gossip regarding the solvency or otherwise of a concern.[1]

Subsequent to 1930, there developed in Ahmedabad a system of long-period deposits, from five to seven years and many mills came to be financed in this manner. A system of 'inter-deposits', i.e. deposits as between one mill and another, also became prominent during the post-depression years: the profits of a mill held in the form of reserves were often 'deposited' with another mill which was believed to be in a sound position. While these new developments made

[1] For a detailed account, see Indian Tariff Board, *Cotton Textile Industry Enquiry*, 1932, Vol. IV.

the danger of sudden withdrawal of deposits more remote, they hampered the proper development of the investment market. This undue reliance on public deposits restricted the supply of good industrial securities, shares, debentures, etc. available for an ordinary investor, and unduly narrowed the market for such investment. Secondly, the losses which occurred in a crisis or panic owing to such money being locked up in almost fixed capital assets, had the effect of discouraging many Indians both from investing in industrial shares and from putting their money in deposit with a bank or with anyone else.[1]

(2) *Private Deposits or Money Provided on Private Account*

While the system of industrial finance through public deposits prevailed in the cotton textile industry of Bombay and Ahmedabad, the method of finding working capital from private deposits or from money on private account provided by one or more of the entrepreneurs, their friends or the managing agents was to be found in most of the medium-sized and comparatively new industrial enterprises in India. Exact figures as to the extent to which private deposits or money provided on private account have contributed to the 'financing' of the various industries are not available, but figures quoted by the Indian Tariff Board in connexion with their enquiries on the match, paper and sugar industries show that, until the outbreak of World War II, these represented between 20 to 30 per cent of the short-term and medium-term requirements of most of the Indian-owned concerns in these industries.[2] In not a few industries, new undertakings were set up with inadequate capital in the hope that once the land had been acquired, buildings constructed and the initial machinery and equipment installed, friends or managing agents would provide the further funds required to keep the enterprises going.

As regards money directly advanced by the managing agents, we have already seen what large sums of money were provided by them in the cotton textile industry of Bombay and Ahmedabad. We shall study the subject of the economic

[1] P. S. Lokanathan, *Industrial Organisation in India*, London 1935.
[2] For details, see S. K. Basu, *Industrial Finance in India*, Calcutta, 1956.

significance of the managing agency system in the industrial organisation of India in a subsequent chapter, but it may be mentioned here that managing agents played quite an important and direct part in the matter of providing industrial finance in India. In the tea industry, firms of managing agents often granted advances against the mortgage of gardens, buildings or machinery or the hypothecation of crops. In the jute industry, on the other hand, the direct assistance of the managing agents was not needed, firstly, because the normal requirements of the industry could easily be met by the issue of additional shares and debentures, and, secondly, because banks were usually willing to offer the necessary accommodation to the jute mills, as the latter had a well-established reputation for efficiency and integrity.

The loans given by managing agents to the concerns they managed were usually given at only $\frac{1}{2}$ per cent above the bank rate and sometimes at par with the bank rate. In the successive crises which overtook the tea and sugar industries during the past twenty years, it was these loans by the managing agents that saved many of the concerns of Bengal, Assam, Bihar and U.P. from ruin. The same thing happened in the coal-mining industry and in some of the under-capitalised concerns in other industries.[1]

Looked at from the standpoint of efficiency, these private deposits and moneys obtained on private account were much more useful to industry in India than public deposits. The danger of sudden withdrawal of deposits was absent in this method of finance, as those who had made the deposits or advanced loans were themselves vitally interested in the concerns and hence preferred to 'see the matter through' rather than withdraw their money. Secondly, as there were no proper banking facilities available for new and middle-sized concerns, such methods of finance were the only solution. Finally, in a period of depression or difficulty, when banks were reluctant to make advances even to fairly solvent concerns, it was these private deposits and money provided on private account by entrepreneurs, their friends and managing agents that helped many of the concerns to pull themselves through,

[1] *Capital*, Calcutta, *Annual Trade and Industry Supplement*, 1958-59.

This method of finance had some drawbacks as well. Very often a managing agent managed a number of concerns and on such occasions, when all the concerns needed financial help, it became too much of a burden for the agent to accommodate all of them. During the difficult period of 1925-30, a number of managing agents in Bombay took upon themselves the work of directly assisting with money *all* the concerns that were under their management, and the task proved far too heavy for them. The managing agency firms themselves were ruined as a result of their bold efforts to bolster up the cotton mills. Secondly, although not to the same extent as public deposits, the system of private deposits also hampered the proper development of the investment market. When industry could depend so much on direct financial assistance by private individuals, it was not unnatural that the ordinary investor from the public did not feel interested in industrial ventures or industrial securities, and tended to retire all the more into his habitually shy groove.

(3) *Indigenous Shroffs or Bankers*

In the past, neither public deposits nor private deposits or private loans were adequate to meet all the various needs of industry in India, and hence industrialists and entrepreneurs often had to approach indigenous shroffs or bankers for financial assistance. While it is difficult to assess to what extent industrial enterprise in India was dependent on the services of this financial agency in the period prior to World War II, certain broad generalisations are possible. Firstly, old and extablished industries (e.g. cotton, jute, and iron and steel) were more or less independent of the indigenous banker, as they could get their capital without much difficulty from either the public or the regular joint-stock banks. Secondly, under-capitalised or small concerns in some of the newer industries (e.g. paper, sugar, match, small tools and implements, etc.) had often to turn to them for finance, as they had no public deposits to fall back upon and their resources by way of private deposits or loans were also extremely limited.

The indigenous bankers (they should be distinguished from moneylenders, pure and simple) had a flourishing

business all over the country during the early years of British rule in India. Political turmoil and incessant wars, however, severely affected their business. The impact of a new economy and changes in the whole basis of India's trade, external as well as internal, hastened their downfall. The creation of Government treasuries and the establishment of banking institutions on western lines operated to their further disadvantage, and with the decrease in the volume of their business, their resources also diminished.[1]

When the small concern resorted to the indigenous banker, it did so partly out of necessity and partly out of preference. The small industrialist had to go to him because he could not get accommodation from any other source. He went to him also because the latter was better acquainted with his means, character, and trading methods: he was content to pay the latter's charges, high though they might be, rather than 'expose himself to the enquiries, the regularised procedure and (as he believed) the greater risks of a joint-bank with a grilled counter and uniformed peon in the doorway.' A regular bank would demand of him a trade bill, a deposit of valuable securities or at least a friend's counter-signature on his promissory note: the indigenous banker, on the other hand, lent on personal knowledge, and often on a simple personal bond, relying on his own acuteness to forestall a possible failure on the part of his debtor. As a result, he had to charge a high rate of interest. Coal companies, for instance, had to borrow money from indigenous bankers at as high a rate as 12 to 18 per cent, and sometimes even at 24 per cent. Industries like leather, tanning, oil mills, rice mills and small tea gardens, had to pay as high as 15 to 20 per cent even when they borrowed on the security of their assets.[2]

The importance of indigenous bankers in the field of industrial finance pure and simple diminished considerably during the past quarter of a century. Some of them have organised themselves into joint-stock banks while others have literally wound up their business. It will be no exaggeration to say that, today, except in the remote areas, where

[1] N. Das, *Essays in Applied Economics*, Calcutta, 1956. Attention is invited to the essay entitled '*The Indigenous Bankers of India*'.
[2] *Indian Central Banking Enquiry Committee Report*, Vol. II.

organised banking facilities are still not available, indigenous bankers do not wield much power or authority as providers of industrial finance. Nowadays, the main concern of the shroff is the provision of short-term credit for trading purposes, although the Bombay Shroffs' Association is reported to have claimed, as recently as 1954, that small industries were obtaining considerable accommodation from them. Even here, the Committee on Finance for the Private Sector referred pointedly to the fact that most of these shroffs did a lot of non-banking business and were unwilling to shed the same. They, therefore, recommended that the question of linking indigenous bankers directly with the Reserve Bank should be pursued only if 'they legally segregated their non-banking business and discarded it within a specified period.'[1]

(4) *Joint-stock Banks*

It is recognised by all students of banking and industrial finance that 'the chief reliance of the average industrial concern for meeting the demands of variations in cash requirements is the commercial bank, which may make a direct loan on the borrower's own rate, or may in effect make the loan by discounting the notes or accepted drafts or trade acceptances of the borrower's customers.' Now, in so far as financial requirements of the major industries are concerned, we may leave out of account the co-operative banks and land mortgage banks. Co-operative banks are concerned mostly with agricultural credit and in the few cases where non-agricultural credit societies have been formed, the beneficiaries are contractors, small traders, artisans, weavers and very small industries. Large-scale industry is completely out of their purview. Land mortgage banks also have got little connexion with industrial finance, as they are mostly engaged in meeting the requirements of agriculturists for long-term credit for the redemption of mortgages of land, for the clearance of debt and for land improvements.

From the standpoint of industrial finance, therefore, the most important agencies today are the joint-stock banks and the loan offices, with the State Bank of India (formerly the Imperial Bank), with its network of branches all over the

[1] *Report of the Committee on Finance for the Private Sector*, Bombay, 1954.

country, at their head. Of some importance also is the Life Insurance Corporation of India which invests its funds in shares and debentures of industrial undertakings.

As we have noted already, the practice of joint-stock banks in India in regard to industrial finance is based largely on the British tradition of commercial banking, under which banks as a rule provide only the working capital requirements of industries on the security of floating assets, and eschew long-term advances against fixed assets. The following table gives an analysis of bank advances as on 30 October 1960, according to their purpose:

	Scheduled banks	*Non-scheduled banks*	*Total*	*Percentage to total advances*
		(In crores of rupees)		
Industry ..	562.8	3.8	566.6	50.1
Commerce ..	395.2	10.0	405.2	35.9
Agriculture ..	6.6	2.1	8.7	0.7
Personal and Professional	96.8	11.8	108.6	9.6
All others ..	38.6	2.4	41.0	3.7
TOTAL ..	1100.0	30.2	1130.2	100.0

It will be seen that, of the total advances of banks amounting to Rs 1130·2 crores, 50·1 per cent or Rs 566.6 crores had been lent to industries.[1] As a matter of fact, since 1953, both the quantity and the relative percentage of advances made to industry have increased.[2]

How are these advances made? According to the Committee on Finance for the Public Sector, although a few banks in India made advances to industries against fixed assets and a few others indirectly partook in long-term industrial finance through (*a*) purchases of shares and debentures of industrial concerns, (*b*) making advances against such shares and debentures and (*c*) investments in the shares and bonds of the Industrial Finance Corporation of India and State Financial Corporations, the share of commercial banks in such financing was relatively small.

This led to a good deal of criticism by industrialists and business men. 'While it is not denied that the first business of commercial banks is to maintain a liquid position so as

[1] *Trend and Progress of Banking in India during the year 1960*, Bombay.
[2] See Appendix XXX.

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to meet all liabilities on time, it should be possible for the scheduled banks to borrow from the Reserve Bank of India against their medium-term or long-term advances. The Reserve Bank should also consider the possibilities of lending to the banks against shares and debentures and fixed assets of industries which are pledged with them as security for loans.[1] Most of the leading banks in India, on the other hand, expressed themselves strongly against any form of direct participation in long-term advances to industries, mainly because the experience of long-term industrial advances by Indian banks had been none too happy in the past.[2]

Prudence dictates that participation by ordinary commercial banks in long-term industrial finance should be exceptional. It is also an established fact that, within the limits of their resources, these banks have been providing finance to all parties *who really deserve them.* Ordinary commercial banks should not be blamed when they say that if long-term advances have to be made, these should be for moderate amounts, in consonance with ordinary banking prudence and consistent with the maintenance of liquidity.

This does not mean that there is no room for improvement. Various suggestions were made by the Committee on Finance for the Private Sector to improve matters in so far as the short-term requirements of industry were concerned. Thus, they said that the Bill Market Scheme of the Reserve Bank of India might be liberalised and so could existing remittance facilities. Subsidies might also be given to banks to open branches in rural areas and adequate security arrangements could be made for banks operating in these areas. Finally, mobile banks could be started which would make banking facilities available even in small villages.

Some of these suggestions have already been adopted by the Central Government and the Reserve Bank of India. Following the submission of a Report by the Committee of Direction of the All-India Rural Credit Survey in August

[1] Memorandum submitted by the Federation of Indian Chambers of Commerce and Industry before the Committee on Finance for the Private Sector, quoted in the Report of the latter.

[2] As recently as during World War II, the failure of a large number of banks in Bengal was attributed, among other reasons, to their long-term advances to industrial concerns.

1954, the Imperial Bank of India was taken over by the State in 1955 and re-named the State Bank of India. In the words of the All-India Rural Credit Survey Report, the objective was 'the creation of one strong, integrated, State-sponsored, State-patterned commercial banking institution with an effective machinery of branches spread over the whole country, which, by further expansion, can be put in a position to take over cash work from non-banking treasuries and sub-treasuries, provide vastly extended remittance facilities for co-operative and other banks, thus stimulating the further establishment of such banks, and, generally, in their loan operations, follow a policy which, while not deviating from the canons of sound business, will be in effective consonance with national policies as expressed through the Central Government and the Reserve Bank'.

Since 1956, the Indian joint-stock banks, with the State Bank of India, as their mentor and guide, have taken further strides in their rôle as resource mobilisers and credit purveyors for the economy. From 1956 to 1959, the magnitude of expansion in bank credit at about 50 per cent was almost the same as that of growth in deposit resources. With the assistance offered by the Refinance Corporation set up in 1958, some of these banks have also started making medium-term loans to industry, thereby providing an integrated credit structure suited to the needs of a developing economy.

Seasonal Requirements of Industry and the Bill Market Scheme

In the thirties of the present century, a good deal of criticism was levelled at the fact that no well-developed and expansive bill market existed in the country. Now, a typical commercial bill is created in this way: a manufacturer, say, a cotton mill, sells goods on three months' credit to a wholesale dealer and, as a preliminary condition of the credit, the dealer accepts a draft drawn on him by the mill. Such a bill is self-liquidating in as much as it arises out of a *bona fide* sale, and has got behind it the backing of goods sold. When the manufacturer is in need of cash, he approaches his bank with a request to discount his bill. If the manufacturer is of good standing, and if the acceptor of the bill is also reputed to

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be sound, the bank gladly discounts such a bill, especially when he knows that the Central Bank would, in its turn, re-discount the bill.

Until lately, this method of obtaining money by discounting bills was not very common and for a variety of reasons. Firstly, the major part of Indian business consisted of agricultural produce, and there was not the same chance to create bills there as in manufacture. 'When crops are marketed, they are sent on their way to the consumer by small merchants through large ones, and it is evident that in practice such small merchants are not in a position to grant credit to the large ones. On the contrary, it is the bigger merchants who often advance money to the smaller traders to buy agricultural produce for themselves.' Secondly, even where commercial bills could be created, the banks were reluctant to discount them, because they could re-discount them only at the Imperial Bank of India, but they did not like that the said bank, their rival in so far as commercial business was concerned, should know their bill portfolios. Thirdly, the system of cash credits was cosidered more convenient both by banks and by borrowers. And hence there was no particular preference on either side for commercial bills as an instrument of credit. Finally, a high stamp duty on bills also acted as a deterrent. [1]

Although the Reserve Bank of India was established in 1935, the facilities for re-discounting bills at the Bank were not accorded to the various joint-stock banks until 1952. Until this latter date, the scheduled banks had been generally raising funds for meeting their seasonal requirements either by the sale of their investments in Government securities to the Reserve Bank or by borrowing from the latter against these securities under Section 17 (4) (*a*) of the Reserve Bank of India Act, 1934. In November 1951, the Reserve Bank of India raised the bank rate from 3 to $3^1/_2$ per cent and also suspended its open market purchases policy—mainly with a view to curbing the inflationary spiral. Simultaneously, as a result of an outcry from the business community, it initiated an alternative mode of accommodation, viz.

[1] S. Bhatter and L. Nemenyi, *The Reserve Bank of India and its Functions*, Calcutta, 1933.

the Bill Market Scheme.[1] The scheme followed in broad outlines the system that prevailed before the establishment of the Reserve Bank under which the Imperial Bank of India could borrow, during the busy season, funds from the Currency Department against internal bills or *hundis* drawn for financing *bona fide* trade or by the conversion of advances granted for the same purpose. During the first year, the scheme was restricted to scheduled banks having deposits of Rs 10 crores or more. The Bank undertook to make demand loans at its banking offices in India to the eligible banks against the security of promissory notes maturing within ninety days, obtained by them from their constituents. This was not exactly a case of re-discounting of commercial bills by the Reserve Bank, but one of making loans to scheduled banks on the lodgement of such bills as security. In order to encourage the bill habit, the Reserve Bank decided to charge interest, on advances under this scheme, at ½ per cent below the Bank Rate and also agreed to bear half the cost of stamp duty incurred in converting demand bills into usance bills, although the duty had already been reduced in 1940 to two annas for every thousand rupees or part thereof. In June 1953, the scheme was extended by the Reserve Bank to scheduled banks having deposits of Rs 5 crores or more and in July 1954, it was further extended to cover all scheduled banks holding a licence, irrespective of the size of their deposits.[2]

Now, the bill market was a common feature of the business and banking system in the U. K. in the days prior to World War I. In the inter-war period, however, the London Bill market was relegated to a secondary place, as, owing to tariffs and trade barriers, international trade had shrunk considerably. The emergence of New York after the first World War as a rival centre of world finance also affected the London Bill market to some extent. With the fall in the bill business, the London Discount market took to the discounting of the British Government Treasury bills, so that it became more or less a market in Government paper.

[1] The scheme was introduced as an experimental measure early in January 1952, but it proved to be so satisfactory that it was subsequently made a permanent feature of the Indian money market.

[2] This last extension was made on the recommendation of the Committee on Finance for the Private Sector.

In India, the bill market did not develop as fast as it should have done—even after the grant by the Reserve Bank of new facilities in 1952. The reasons were as follows. Firstly, the bulk of the financing of foreign trade was done by foreign banks, commonly known as the Exchange banks. The majority of both the export and import bills were drawn in sterling and such bills were obviously not suitable for negotiation in a bill market in India. Further, in the absence of any Acceptance Houses in India, export bills were invariably payable outside India and hence were not good for sale in this country nor eligible for re-discount with the Reserve Bank. The import bills, on the other hand, were for small amounts and hence were not helpful in promoting a bill market. Secondly, in the case of movement of goods within the country, it was still customary for the seller to extend an open account credit rather than draw a bill. Even banks preferred giving cash credit or overdraft against the storage of goods pending movement rather than accept a bill, as they could, in the former case, recall the advance at short notice in case the borrower's financial position was adversely affected. In the case of a bill, they had to wait until its maturity.

We thus see that the Bill Market Scheme as framed by the Reserve Bank departed from the traditional method of re-discounting of bills. Under this arrangement, short-term credit was advanced to meet the *bona fide* requirements of trade and industry, permitting the banker at the same time to make withdrawals and repayments into the account as often as he liked. As the scheme provided for advances and not re-discounting facilities, the banks were able to minimise interest charges by borrowing according to their needs and by remitting spare funds to reduce their indebtedness.[1]

The Bill Market Scheme has now been in operation for nearly a decade. While during the earlier years of its inauguration, the scheme was being increasingly utilised by banks, there has been a marked decline since 1956-57, due largely to a material increase in the resources of banks as well as in their investments in Government securities. The following

[1] Article on '*The Bill Market Scheme in India*' in the *Reserve Bank of India Bulletin*, September, 1953.

table illustrates the rapid decline in the use of Bill Market facilities during the last four years.[1]

Amounts Borrowed by the Banks under the Bill Market Scheme

(In crores of rupees)

	1956-57	1957-58	1958-59	1959-60
Aggregate amount of limits sanctioned ..	185.40	137.41	114.00	54.27
Maximum outstanding borrowings during the season	73.79	32.42	13.67	15.21

Two explanations have been offered for the failure of the Bill Market Scheme to live up to the expectations of its framers. Firstly, there appears to be a reluctance to use the Bill as a means of raising finance when cash credits and overdrafts are not difficult to get. 'The Bill has its uses, and shows its strength, only in times of credit stringency.' Secondly, the setting up of specialised financial institutions to fill up certain 'gaps' in the credit structure, has made the Bill Market Scheme somewhat redundant. The efforts that are being made to harness the co-operative agency and even the State Bank of India to provide credit to small units and the Guarantee Scheme of the Reserve Bank of India under which it shares with commercial banks the risks they face in meeting the financial requirements of small-scale industries, have also led to the belief that 'there is no innate superiority in the special form of credit represented by bills.'

The Rôle of Special Institutions

As has been stated in a preceding section, the share of commercial banks in the long-term financing of industry has been rather small in this country. We have also seen in an earlier chapter how, even in the U.K., special institutions have been set up, over the past twenty years or so, to meet the long-term requirements of particular classes of industry. On the Continent also, notwithstanding the tradition of 'mixed banking' which held sway, it has been found necessary to set up institutions dealing exclusively or mostly with the long - and medium-term requirements of industry. The

[1] *Reserve Bank of India Bulletin*, Bombay, June, 1961.

Industrial Mortgage Banks of Finland, Hungary and Saxony and the National Economic Bank of Poland were typical examples of such efforts. In Canada also, an Industrial Development Bank commenced operation in November 1944, while a separate Industrial Finance Department was created in 1946 in Australia within the Commonwealth Bank of that country. Similar developments have taken place in the comparatively under-developed Latin American countries as well. 'Fomento' credit organisations of specialised institutions to assist in the mobilisation of capital for production purposes and to provide long-term cerdit to industries have been set up in Mexico, Brazil, Chile, Argentina and Colombia, mostly during the years following the end of the second World War.[1]

What is the *raison d'etre* for establishing such special institutions for the provision of long-term industrial finance? The main reason is that, on the one hand, the ordinary joint-stock banks cannot afford to lock up their capital and other assets in long-term projects and, on the other hand, until lately, there was an unwillingness, for various reasons, on the part of the average investor to subscribe readily to shares or debentures floated by industrial companies. While the mobilisation of domestic capital as well as the development of a capital market which would ensure a regular flow of new money into industries at a reasonable rate of interest, is necessarily a long-term process, corporations, in which the Government, the central banks, commercial banks and insurance companies and other financial institutions can all participate, help to stimulate industrial development and ensure that capital flows into the most productive channels.

The Industrial Finance Corporation of India

The first specialised institution to be set up in this country was the Industrial Finance Corporation of India. Established under a special Act in 1948, the Corporation makes medium and long-term credits more readily available to industrial concerns in India, particularly in circumstances where normal banking accommodation is inappropriate or recourse to capital issue methods is unpracticable. The authorised capital of the Corporation is Rs 10 crores, divided

[1] N. Das, *Studies in Indian Economic Problems*, Calcutta, 1954.

into 20,000 fully paid-up shares of Rs 5,000 each. To start with, 10,000 shares of the total value of Rs 5 crores were issued. Of the capital issued in the first instance, the Central Government and the Reserve Bank subscribed 2,000 shares each; scheduled banks subscribed 2,500 shares; investment trusts, insurance companies and other similar financial institutions another 2,500 shares, and co-operative banks, 1,000 shares. The capital structure of the Industrial Finance Corporation of India is thus neither wholly owned by the Central Bank nor wholly independent of State ownership and control.[1]

As regards investible funds, besides the share capital, the Corporation is authorised to issue bonds up to five times the paid-up capital and to accept deposits from the public repayable after not less than five years. The shares of the Corporation are guaranteed by the Central Government as to both repayment of principal and payment of the annual dividend at a minimum rate fixed by Government by notification at the time of issuing the shares.[2] In the same manner, the bonds and debentures of the Corporation are guaranteed by the Central Government in respect of the repayment of the principal and payment of interest.

The inadequacy of the capital structure was criticised by many at the time the Bill was being debated in the legislature. It was argued that, even with the use of its borrowing powers, the resources of the Corporation would be very meagre and totally inadequate for securing the rapid industrialisation of the country. 'It will have a paltry amount of Rs 50 crores where hundreds of crores are required.' But the critics entirely missed their mark. Firstly, it was never intended that the Corporation would pour out its funds for every category of industry or every type or requirement. The Corporation is designed merely to *supplement* the capital needs of industry and to assist only such industries as are unable to raise the additional capital in the open market.

[1] The capital structure of the Industrial Finance Corporation of India has been criticised in some quarters as affording no opportunity to private individuals to become its shareholders. But there is no special reason why private individuals must necessarily be permitted to hold shares in an institution of this kind. Anyway, this 'lacuna' has been made good in the case of State Financial Corporations.

[2] The guaranteed dividend was fixed at 2½ per cent.

Secondly, for a long time, it had difficulties in investing even a much smaller sum than Rs 50 crores.

The Corporation can finance 'industrial concerns' only. This has been defined under the Act to mean any public limited company or co-operative society incorporated by an Act of the legislature and registered in India and engaged in the manufacture or processing of goods or in mining or in the generation or distribution of electricity or any other form of power. By an Amendment Act in 1952, the scope of the Corporation's activities has been extended to cover 'companies engaged in shipping' as well.[1]

The Corporation can transact the following kinds of business: (*a*) guaranteeing loans raised by industrial concerns which are repayable within a period not exceeding 25 years and which have been floated in the open market; (*b*) underwriting the issue of stocks, shares, bonds or debentures by industrial concerns; (*c*) granting loans or advances to, or subscribing to debentures of, industrial concerns, repayable within a period not exceeding 25 years. No accommodation is, however, to be given under (*a*) and (*c*), unless it is secured by a sufficient pledge, mortgage, hypothecation or assignment of Government or other securities, stocks, shares, or secured debentures, bullion, movable or immovable property or other tangible assets. Further, the Corporation must not enter into any arrangement under (*a*) and (*c*) with a single industrial concern for an amount equivalent in the aggregate to more than 10 per cent of the paid-up share capital, and in no case exceeding Rs 50 lakhs.[2]

A good deal of criticism was levelled at the Corporation in 1953-54 about the manner in which it disposed of its loan applications. Charges of nepotism and partiality were laid at the door of the management and so much public passion was roused that the Government of India was compelled to set up a Committee of Enquiry. This committee made an

[1] Further amendments are in contemplation to cover other sectors of private enterprise.

[2] The underlying object of putting such a limit on the accommodation was to ensure diversification of the risks of investment. The limit was soon raised to Rs 1 crore, as it was felt that the limit of Rs 50 lakhs rather inadequate. As a matter of fact, the Corporation can now make advances even exceeding Rs 1 crore to a single concern, if the loan is guaranteed by the Government of India.

exhaustive analysis of the loans sanctioned by the Corporation up to date and submitted a report to Government in May 1953. The Report exonerated the management from charges of favouritism, but said that some at least of its advances were unhappy and could have been avoided.[1]

The Industrial Finance Corporation Enquiry Committee made a number of suggestions on matters of policy which may well bear repetition. For example, it suggested that (*a*) no loans shall ordinarily be granted in respect of industries where 'the saturation point' has been reached, (*b*) Government should issue directives to the Corporation regarding the principles to be followed by the latter in granting loans, (*c*) Government should give to the Corporation a clear indication as to which regions should be treated as backward, with a view to enabling the Corporation to give a preference to such areas and (*d*) the Corporation should not participate in equity or risk capital until the Reserve Fund of the Corporation has aggregated to Rs 5 crores. Most of these recommendations were accepted by Government. It is pertinent to point out, however, that the Industrial Finance Corporation represents a new experiment in the field of industrial finance, and principles can be evolved and practices established only in the light of experience.[2]

An important lacuna in the Industrial Finance Corporation Act of 1948 was that it could make advances only to industrial concerns *already engaged* in business: it could not make any advances to concerns which were *about to engage* in business. This was rectified by the Industrial and State Financial Corporations (Amendment) Act of 1955, which received the assent of the President on 10 September 1955.[3]

Another criticism of the working of the Industrial Finance

[1] As a result of the public agitation, the then non-official Chairman (Mr. Shri Ram) had to resign on 14 February 1954 and his place was taken by a senior official of the Government. Later, the Act was amended so as to provide for a full-time Chairman who could devote all his time and attention to the affairs of the Corporation. The first full-time Chairman (Mr. K.R.K. Menon) took office on 6 August 1955.

[2] Seventh Annual Report of the Industrial Finance Corporation of India for the year ending on 30 June 1955.

[3] The Committee on Finance for the Private Sector also made certain suggestions with a view to making the Corporation a more useful instrument of industrial finance. It pointed out that there was avoidable delay in sanctioning loans, that the terms for loans were often unduly harsh and that the rates of interest charged were sometimes on the high side.

Corporation of India is that it does not provide equity or risk capital. There is no legal bar to the Corporation's undertaking this type of financing (the Corporation is empowered to underwrite shares under Section 23 of the Act), but this has not been attempted in actual practice, mainly because, under the Act, the Corporation had to dispose of any such shares within a period of seven years. The Committee on Finance for the Private Sector recommended that this limitation should be removed and the Amendment Act of 1955 liberalised the Section by saying that the stocks, shares, bonds or debentures acquired could be retained, with the permission of the Central Government, even beyond the period of seven years. The industrial Finance Corporation Act was again amended in 1960 so as to enable the Corporation to guarantee (*i*) loans raised by industrial concerns from scheduled banks or State Co-operative Banks, (ii) deferred payments in connection with the purchase of capital goods manufactured in India and (iii) loans raised from or credit arrangements made by industrial concerns with any bank or financial institution outside India in foreign currency. Up to the end of June 1961, the Corporation underwrote issues to the tune of Rs. 4.2 crores. This is not a very big amount, but it should not be forgotten that the IFC took to this business only three years ago.

In recent years, the lendable resources of the Corporation have been augmented by (*a*) the issue of bonds, (*b*) borrowings from the Central Government and (*c*) loans from international agencies like the U.S. Development Loan Fund. The total amount of bonds outstanding at the end of June 1961 was Rs. 42.35 crores, while the outstanding borrowings from the Central Government amounted to Rs. 15.25 crores. The Corporation sanctioned during this year loans in foreign currency equivalent to Rs. 4.3 crores, for the first time since its inception in July 1948.

Up to the end of June 1961, the Corporation had distributed a total amount of Rs. 105.82 crores as loans and advances to industry. A study of the distribution on loans according to the nature of industry shows that the IFC has been following a balanced policy in assisting the 'consumer goods' industry as well as the 'producer goods' and the 'intermediate

goods' producing industry. Of the total loans, Rs. 76.55 crores went to 152 new undertakings and Rs. 29.27 crores to 87 old undertakings for renovation, modernisation and expansion.[1]

State Financial Corporations

The Industrial Finance Corporation of India caters primarily for the needs of large-scale undertakings: its clientele is also restricted to public limited companies. But the smaller and medium-sized industries have problems of their own and special institutions are required to cater for their requirements. So, in 1951, the Government of India placed on the Statute Book a State Financial Corporations Act. Under the Act, the States could set up local Financial Corporations with a view to providing medium and long-term credit to small - and medium-sized industries which fell outside the purview of the Central Corporation.

The Act, though closely patterned after the Industrial Finance Corporation of India Act of 1948, made three important departures. Firstly, the designation of 'industrial concern' was widened to cover private limited companies, partnerships and even proprietary concerns. Secondly, members of the public and even non-scheduled banks were permitted to subscribe to the share capital of State Corporations.[2] Thirdly, State Financial Corporations could give guarantees and make loans and advances for a period of not more than 20 years as against the 25 years of the Central Corporation.

Since the passing of the Act in 1951, State Financial Corporations have been set up in every State in the Indian Union.[3] These Corporations are miniature editions of the Corporation at the Centre. Under the Act, the maximum authorised capital of a State Corporation can be Rs 5 crores. It can also issue bonds and debentures like the Central Corporation, but the total amount thereof must not exceed five times the amount of the paid-up share capital and reserve

[1] Thirteenth Annual Report of the Industrial Finance Corporation of India for the year ended 30 June 1961.

[2] The number of shares allocated to such parties has, however, been restricted to 25 per cent of the total number of shares.

[3] The latest to appear on the scene were the Corporations in Mysore, Gujarat, and Jammu and Kashmir, which were established in 1960 only.

funds of the Corporation. It may also accept long-term deposits from the public under certain terms and conditions.

Since their inception and up to the end of March 1961, the total amount of loans sanctioned by the various State Financial Corporations was Rs 36.2 crores and the amount disbursed was Rs 22.16 crores. The total amount of loans and advances outstanding was Rs 17.1 crores. The discrepancy between the loans sanctioned and those actually disbursed is said to be due to the fact that the conditions no which loans are sanctioned are sometimes so rigid that many applicants find it difficult to accept them. On the other hand, during the period 1958, 1959 and 1960, the average total amount of loans outstanding of all the Corporations was approximately Rs 11.14 crores as against the average amount of loanable funds of Rs 19.41 crores. In other words, the Corporations were able to utilise only 57.3 per cent of their resources. As a consequence of the low utilisation of resources, many of these Corporations are faced with deficits in their earnings which compel them to rely heavily on the State Governments for meeting their dividend liability.

For this state of affairs, the Corporations cannot be held responsible. It appears that although innumerable applications are received, a majority of the applicants do not furnish the necessary information in respect of the installed capacity of their plant and machinery, annual production, estimated increase of output as a result of the proposed expansion, cost of production and their annual profit and loss accounts. The result is that many applications have to be rejected outright. Secondly, State Corporations have to deal not only with corporate concerns but also with partnerships and proprietary concerns including joint-family businesses. It has been found from experience that many concerns offer properties for which the relevant documents of title are not available or there are complications which have to be removed before the title can be accepted as clear and marketable.[1] As has been stressed by the Board of Directors of the punjab Financial Corporation, an organised system of industrial banking must demand a minimum standard of working efficiency and book-

[1] Fifth Annual Report of the Bombay State Financial Corporation for the year ended 31 March 1958.

keeping system on the part of the borrowers, but unfortunately many of the applicants show considerable reluctance to disclose full facts of their affairs or to take the Corporation into their confidence.[1]

Other difficulties which these State Financial Corporations have to contend with are that many borrowers ask for advances solely against stock in trade: this, however, is the normal function of commercial banks and is outside the scope of the activities of a Financial Corporation, its main function being to grant advances, whether for capital expenditure or for working capital, against block assets comprising land, buildings, plant and machinery. Another problem which presents itself to these Corporations is that statistics in regard to the various industries are not readily available, and, in the absence of such information, it becomes extremely difficult to make a proper assessment of the scope and prospects of an industry.[2]

The Industrial Credit and Investment Corporation of India, Ltd.

This is a privately owned and managed Corporation set up in 1954, but it had the blessing of the Central Government from the very outset. Some time in 1953 a three-man Mission sponsored by the Government of India and the World Bank decided that what the country needed was a special institution of the type of the Industrial and Commercial Finance Corporation of the U.K., as, because of its quasi-Government character, the Industrial Finance Corporation of India had not been able to meet the long-term requirements of industry as effectively as it should have done.

The Corporation was launched with a paid-up share capital of Rs 5 crores, subscribed wholly by domestic and foreign private investors, with the former holding about 70 per cent of that capital. In addition to the share capital, the working funds of the Corporation consist of an interest-free deposit of Rs 7½ crores advanced by the Government of India out of the Technical Corporation Administration rupee counterpart funds. Finally, the Corporation was granted by the World Bank

[1] Sixth Annual Report of the Punjab State Financial Corporation for the year ended 31 March 1959.

[2] Fifth Annual Report of the West Bengal State Financial Corporation for the year ended 31 March 1960.

a long-term loan of Rs 5 crores, guaranteed by the Government of India. The initial working capital of the Corporation thus amounted to Rs 17½ crores, but it was empowered to borrow up to three times the total amount of its paid-up capital plus the Government deposit.

With these resources (at the end of December 1961, its investible resources had increased to more than Rs 44 crores), the Corporation has undertaken, among other things, direct lending and investment, underwriting of issues, and provision of technical and managerial aid to the private sector. There is no direct Government participation in the management of the Corporation except that Government appoints one Director on the Board and also the Chairman.

Since 1955, the activities of the ICICI have been steadily on the increase. The total of proposals sanctioned, till the end of December 1961, was Rs 42.71 crores, although Rs 24.3 crores out of this had not been actually availed of. Because of its access to foreign exchange facilities through the World Bank, the ICICI has facilitated the purchase of capital goods from abroad by industrial enterprises in India. With its readiness to underwrite new capital, this Corporation has set a new tradition in the building up of the Indian capital market.[1]

National Industrial Development Corporation

This State-sponsored Corporation, with capital provided entirely by the Government of India, was also launched in 1954. This Corporation represents an effort to tackle the problems of industrialisation and unemployment in the country from the angle of shyness of capital and enterprise. There are important sectors where, for various reasons, private capital and enterprise are not coming forward at all. The National Idustrial Development Corporation starts new industries in these sectors and manages them through the initial process of development till they reach the stage of earning profits. At that stage, they can be handed over to private enterprise, if considered necessary and desirable.

[1] Of the total accommodation granted by the ICICI till the end of 1961, 69% were in the form of loans and guarantees, 24% were in the nature of under-writing operations in respect of ordinary and preference shares and debentures, and 7% in the form of direct subscriptions to ordinary and preference share issues.

It may be stated here that the NIDC does not enter into competition with industries already well established in the country. Instead, it explores the possibilities of developing new industries and selects schemes to be taken in hand. If private entrepreneurs are forthcoming for the establishment of such units, the Corporation helps them on the technical side as well as through participation in financing the units. Alternatively, the Corporation itself establishes and operates new industrial units. The NIDC is conceived mainly as an instrument for securing a harmonious development of industries in both the public and private sectors. It does not undertake the financing of industries except in so far as this becomes incidental to the development of certain special categories of industries.[1]

In actual practice, however, the National Industrial Development Corporation has confined its activities mostly to the granting of loans for the modernisation and rehabilitation of the jute and cotton textile industries. At the close of March 1961, the total amount sanctioned for the purpose was Rs. 19.59 crores, although actual drawals by the mill companies aggregated to only Rs. 6.58 crores or 34% of the total loans sanctioned. While it is true that the Corporation has also investigated the problems of a few other industries (e.g. iron foundries and forges, fabrication of steel structurals and manufacture of printing machinery and wood pulp), the financial assistance sanctioned for such industries has been negligible.

The operations of the NIDC have been criticised in certain quarters on the ground that it appears to have been set up primarily for the rehabilitatoin of the cotton textile and jute industries. 'It is not understood why modernisation of cotton and jute mills is singled out for financial assistance by a special corporation. The other financing corporations are well able to make loans to them. The NIDC should be left with the more important task of promoting new industrial enterprises for which it is perhaps better suited.'[2]

[1] N. Das, *Studies in Indian Economic Problems*, Calcutta, 1954.

[2] H. T. Parekh, *The Future of Joint-Stock Enterprise in India*, Bombay, 1958. Lately, the NIDC has set up a subsidiary company under the name 'Pyrites and Chemicals Development Co. Private Ltd.', for the implementation of a project for the production of sulphur from pyrites.

Life Insurance Corporation of India

In every country (and no less in India) life insurance companies invest a substantial portion of their funds in industrial shares and debentures, thereby helping economic development. Life insurance was nationalised in India in 1956, and the entire business was taken over by a single organisation called the Life Insurance Corporation of India.

Although under Section 27A of the Insurance Act, a minimum of 50% of the investment is required to be made in Central and State Government Securities and in issues of public corporations such as Municipalities, Port Trusts, etc., the Corporation has got such huge funds at its disposal that, even with the restrictions imposed under the Insurance Act, it can play a decisive rôle in the capital market. Much more important than even the volume of operations, however, is the fact that, as an investor having large funds ready for investment, its investment activity can exercise a considerably stabilising influence. It follows, therefore, that the responsibility of the LIC for judicious investments is very heavy. On the one hand, by reason of its substantial ownership of shares in joint-stock companies, the Corporation must act as a watch-dog of corporate enterprise in the country. On the other hand, with the resources at its command, it can play as important a rôle in the new issue market as it is able to play in the stock market. An analysis of the investments made by the LIC since its inception shows that these are fairly well distributed over the entire private sector and that it has not hesitated to underwrite new issues, as long as these were found to be generally sound.[1]

Refinance Corporation of India

Another institution called the Refinance Corporation of India was constituted in 1958 to enable selected commercial banks to provide medium-term finance to industrial concerns. The question arose how the funds, which had accrued from the sale of surplus agricultural commodities under P.L. 480 should be utilised and, as a result of discussions between the U. S. and Indian Governments, a permanent organisation was set up in the form of the Refinance Corporation of India.

[1] Vide Appendix XXXI.

Since its inception in June 1958 and up to the end of December 1961, the Corporation sanctioned loans to the extent of Rs. 11.16 crores. The operations of the RCI are hampered by the fact that it can provide refinance for a medium term only, viz. three to seven years. Recently, however, the Corporation has decided to consider, in exceptional cases, loans for a longer period up to ten years. This combined with extension of its refinancing facilities to a number of smaller commercial banks, State Financial Corporations and State Co-operative Banks has considerably widened the base of its operations.

Assistance to Small Industries

Mention should also be made of the National Small Industries Corporation set up in February 1955, not only to finance small industries but also to tackle their special problems of marketing, techniques of production, management, and supply of raw materials and machinery. This is a wholly State-owned undertaking, financed by loans and grants from the Central Government. The most important activity of the NSIC is to secure orders from Government purchasing agencies on behalf of small-scale units and to supply machines to the latter on the hire-purchase system.

It may be mentioned in this connection that the State Bank of India also has a scheme for the co-ordinated provision of credit facilities to small industries. This was initiated in April 1956 and extended to all its branches with effect from January 1959. In January 1959, an agreement was reached by the National Small Industries Corporation and the State Bank of India on the subject of grant of advances by the latter to small units up to the full value of raw materials when they had secured firm orders from Government and quasi-Government bodies.

Another scheme for rendering assistance to small industries has been formulated in pursuance of the recommendations made by the Seminar on Financing of Small-Scale Industries in India, organised by the Reserve Bank of India in July 1959, in Hyderabad. This is a guarantee scheme for advances to small industries. The object of the scheme is to grant a degree of protection to the lending institutions (espe-

cially State Financial Corporations) against possible losses incurred by the latter in respect of such advances. Losses would be shared between the lending institutions and the Government of India, subject to the condition that the maximum amount recoverable against the guarantee issued under this Scheme in respect of any one advance will not exceed Rs 1 lakh.[1] This scheme was brought into force on July 1, 1960. Since August 1961, the scheme has been extended to cover "risk participation," particularly in respect of co-operative institutions.

Investment Trusts

In the institutional field, one major gap which still exists is the absence of Investment Trusts which play so important a part in other countries in providing industrial capital. An Investment Trust is 'an agency for the co-operative buying and selling of securities for a group of associated investment beneficiaries'. Its main characteristic is that it enables the investor, through a simple commitment, to diversify his investments over a large number of securities and thereby reduces the risks of capital depreciation and poor dividends. Also, the investor obtains the services of expert knowledge and management available with the Investment Trust.[2]

In the U.K. and U.S.A., the number of Investment Trusts is around 270 and 170 with total funds of £560 million and $ 11 billion respectively. These organisations have developed much later in India than in either the U.K. or the U.S.A. The reasons for the late development of the movement lay basically in the low volume of savings available for investment, and also partly in the absence of adequate investment outlet, conducive to the promotion of Investment Trusts. The first important Trust was the Industrial Investment Trust, Ltd., registered in 1933 at Bombay, with an authorised capital of Rs 2.5 crores and a paid-up capital of Rs 1 crore. A few more such Investment Trusts were established in 1936 and, in the following year, the House of Tatas launched the Investment Corporation of India, Ltd. Many of

[1] *Reserve Bank of India Bulletin*, June 1960.

[2] For a detailed account of Investment Trusts and their operations, the reader is referred to an article on the subject, published in the *Reserve Bank of India Bulletin*, October 1960.

these Investment Trust companies were, however, of the 'bucket-shop' variety, promoted to collect public money mainly for employment to the advantage of the promoters and directors in their speculative share operations. With the break in prices in 1937, most of these companies went into liquidation. During World War II years, there was a further impetus to the Investment Trust movement mainly because of the interest evinced by a number of managing agents. In March 1959, the total number of such companies was 595 with a paid-up capital of Rs 37.7 crores, as compared with 122 companies with a paid-up capital of Rs 15.2 crores in March 1956.

Many of these Investment Trusts do not, however, function as independent investment trusts, in the accepted sense of the term. Being closely associated with managing agency houses, these companies were made use of mainly to finance or control companies in which the managing agency houses were directly interested. In a sense, these were the same managing agencies under a different name, and were, in effect, more akin to 'finance companies' or 'holding companies' than to Investment Trusts. The basic objective of an Investment Trust, viz. independent selection of investments purely on merits with due regard to safety and diversification, was not served. According to a study made by the Reserve Bank of India of the annual reports, balance sheets and other accounts of 32 such investment companies, the pattern of investments even in 1959 reflected their association with managing agency or other industrial groups. In the case of several companies, such investments were spread over a few companies only, the shares of some of which were not even quoted on the stock exchanges. By and large, there was little evidence of disinterested diversification of investments, the two notable exceptions being the Industrial Investment Trust, Ltd., and the Investment Corporation of India, Ltd.

The conclusion is, therefore, inescapable that although there are a number of Investment Trusts in operation, they are not 'independent' investing agencies in the sense in which such Trusts operate in the U.K. and the U.S.A. As a result, their contribution in the matter of mobilising savings

and diversifying industrial development has been rather limited.

A Résumé

We thus see that since 1947 there has been a considerable spurt of activity in the sphere of industrial finance. A number of Investment or Development Corporations have been set up, either with direct participation by the State or with its blessing, to meet the various requirements of industry. The entrepreneur in the private sector has now a wide selection of institutions to which he can turn: he can no longer complain that the available credit mechanism is defective or inadequate. The country has travelled a long way from the days when the Indian Central Banking Enquiry Committee submitted its Report. If private industrial enterprise is still 'under a handicap' today, the causes thereof must be sought in spheres other than those of finance.

Chapter IV

THE MANAGING AGENCY SYSTEM AND ITS RÔLE IN THE FINANCING OF INDUSTRY

It has been universally recognised that the seccessful financing of an enterprise depends on sound and efficient management, but nowhere is the truth of this statement as pointedly demonstrated as in India. The managing agency system arose in India during the latter part of the nineteenth century, and this system of organisation and management gradually spread to almost all industrial enterprises—Indian as well as British.[1] The rise of the managing agents was due to the fact that they filled the rôle of promoters and pioneers in many of the newly established industries in India; they came into prominence because it was they and they alone who could supply a regular team of trained and efficient managers; and they gathered power as they found that the capital market was shy, and that industry looked to them for financial aid, both direct and indirect. The continuance and prevalence of the managing agency system has been due more to this last factor than to any other. Banks were not prepared to finance the long-term needs of industry, and were unable to provide anything more than 'circulating capital' and that also for short periods; on the other hand, many of the enterprises were under-capitalised at the very outset, and needed financial assistance or guarantee at every stage of their work. So the managing agency system came to dominate Indian industry. As has been aptly stated by the Company Law Committee, 'history, geography and economics all combined to create and develop a system which, in some of its distinctive features, still retains its unique character.'[2]

Historically, the home of the managing agency system was in Calcutta from where it spread to other parts of India. Between 1830 and 1880, a number of British traders operating in the eastern part of the country interested themselves in

[1] For a detailed account, see P.S. Lokanathan, *Industrial Organisation in India* London, 1935.

[2] *Report of the Company Law Committee*, New Delhi, 1952.

the development of such industries as jute, plantations and mining. They imported some capital from abroad, but the rest came from themselves and their friends and associates in India. They would then export the products of these primary and extractive industries to their principals in the mother country. In the course of time, they extended their activities to other fields like shipping, sales agencies and investment trusts.

The same organisational pattern was followed when, in Bombay and Ahmedabad, some Indian business men, having accumulated large funds in trading operations, decided to develop the cotton textile industry. It was during the latter part of the nineteenth century and the first decade of the present century that many of the larger Indian managing agency houses were established. The *Swadeshi* movement gave a further stimulus to the development of these houses, while the boom in company floatations in the years after World War I enabled them to branch out into new spheres. It was at this stage that the managing agency of the Tatas appeared on the scene and embarked on the hitherto untrodden fields of heavy industry and public utility undertakings.

These managing agency houses, European as well as Indian, also played a leading part in the formation of the early joint-stock companies. Although a systematic record is lacking, it is surmised that a substantial number of the 505 joint-stock companies reported to have been in existence in 1882 had been formed by various managing agency firms. Even as late as 1936, a majority of the joint-stock companies newly floated had to be sponsored by the better-known managing agency houses.[1]

Managing Agency System sustained by lack of a properly organised Capital Market

We have seen already that, until 1947, the country lacked a properly organised capital market. An integrated capital market, with issue houses or investment syndicates occupying a central position in it, provides the main channel through which private investments are made in most advanced countries of the world. In India, these functions were carried out largely

[1] Raj K. Nigam, *Managing Agencies in India*, New Delhi, 1958.

by the managing agents, who were thus able to entrench themselves in a very strong position in the private sector of the country's economy. It could even be argued that their existence was, in itself, an impediment to the growth of an organised capital market.

The financial assistance rendered by managing agents has been both direct and indirect. In a previous chapter, we have noted instances of direct financial aid rendered by managing agents to the concerns they manage. Here we shall consider some further aspects of managing agency finance as prevalent in India.

Ever since the system came into existence, managing agents (particularly in Bombay and Ahmedabad) started the practice of purchasing the shares of the companies they managed in the names either of themselves or of their friends, and even took up debentures floated (often by themselves) by those companies. In Calcutta and Madras, on the other hand, where the managing agency firms were the inheritors of the tradition of the early European Agency houses, many of them carried on a large banking business in addition to their other activities. There were many instances of firms investing their funds in several industrial concerns and some of the leading managing agents (e.g. Messrs. Andrew Yule & Co., Ltd., of Calcutta) hardly ever borrowed money from any joint-stock or exchange bank to finance the companies they looked after.

Equally important were the various indirect methods by which managing agents assisted the financing of industries. These had resulted partly from the methods employed by banks in granting loans to industry and partly from the fact that, apart from the managing agents, there were no important entrepreneurs who could get the confidence either of the investing public or of the banks. We shall consider these various indirect methods one by one.

We have seen that, until lately, joint-stock banks in India were very rigid even with regard to the grant of short-term credit. They made advances only against tangible and marketable securities lodged or pledged with them and in addition or alternatively they wanted the several responsibilities of at least two persons or firms unconnected with each other in general partnership. These practices compelled the managing

agents to come forward and give the necessary guarantees to the banks. Except in Calcutta, for instance, most banks up-country and in Bombay insisted on the signature of the managing agents even when goods were hypothecated; and when goods were not hypothecated, the guarantee of the managing agents on notes of hand, in addition to the signature of a director of the company, was insisted upon.[1] This rather exacting requirement was defended by bankers on the ground that 'the banker cannot know at any given time what the exact financial position of the company is, and he has greater confidence in the agency firm, and is willing to advance only on the guarantee of the agents.' It was indeed unfortunate that banks in India were not willing to take the reasonable risks they often did in other types of lending operations and, by their rigidity, helped to strengthen the hold of managing agents on industrial enterprise in India.

Even with regard to public deposits which formed such an important source of finance to the cotton textile industry, it was the name of the managing agents that ensured a steady flow of deposits. In Ahmedabad, for instance, deposits were automatically renewed for years together in those mills which were controlled by reputed firms of managing agents. On the other hand, during the depression of 1929 and after, public deposits were withdrawn from those concerns where managing agents were reputed to be inefficient, lazy or dishonest.[2]

In the matter of issue of shares and debentures also, the standing and reputation of managing agents largely determined the success or failure of the issue. Even a very cursory analysis of Indian industrial history shows that, in the early stages of pioneering of industry in India, it was the managing agents who 'drew out' capital from the small class of investors that existed. Even in will-established industries like cotton, jute, coal, or iron and steel, the promotion of a concern without the backing of a big firm of managing agents, was very difficult, if not altogether impossible.[3]

The question has repeatedly been asked why industry in

[1] Indian Tariff Board, *Cotton Textile Industry Enquiry*, 1927, Vol. IV.
[2] Indian Tariff Board, *Cotton Textile Industry Enquiry*, 1932, Report.
[3] S. K. Basu, *The Managing Agency System*, Calcutta, 1958.

India was so utterly dependent on managing agents for its finance. As has been hinted already, this dependence was the result of certain big gaps in the economic system of the country. Three broad reasons may be mentioned. Firstly, the Indian investor was notoriously shy, and did not, until very recently, care to invest his capital in debentures or shares as did the investor elsewhere. Secondly, in India there were neither issuing houses nor securities companies which in other countries float new concerns and take up the risks in the initial stages, nor did our banks pursue a policy sympathetic and elastic enough for the varied needs of industry. Finally, there was a general tradition in the country, from the time of its early industrial beginnings, that the financing of industry was the privilege and duty of private managing agency firms. It was only when the burden of finance became heavy that people began to wonder whether it was inevitable that industry must look to the managing agents for all help, inspiration, and guidance.

The Cost of the Managing Agency System of Finance

The managing agency system has been assailed from various quarters for its alleged inefficiency, and the opportunity it has given for lazy or fraudulent management, but very few people have attacked the system on the score of its financial policy. One writer has suggested that the system of managing agency finance revealed certain characteristic defects. He has stated that, owing to the prevalence of the managing agency system of finance, industry came to be dominated too much by financial considerations, and too little by industrial ones; he has further asserted that, owing to the managing agency system of industrial finance, no mill company was able to develop its own system of financing independently of the managing agents; and finally, according to him, the managing agency system of finance led to enormous speculation in the shares of cotton mill companies.[1]

The present writer is not an apologist for the managing

[1] P. S. Lokanathan, *op. cit.*, pp. 225-8. The present writer, however, agrees with Dr. Lokanathan that many managing agents in India were inefficient, and their services costly, in the sense that they were not technical experts and that they paid too little consideration to such matters as modern machinery, organization, and marketing.

agency system, but he believes that the financial policy of the managing agents was their least objectionable feature. When it is said that, under the managing agency system of finance, industry was dominated too much by financial considerations and too little by industrial ones, and it is pointed out that in the cotton textile industry of Bombay and Ahmedabad, transfers of agency often took place because one firm happened to be less solvent financially than another, it should not be overlooked that this would have become more or less inevitable under any form of management. Similar instances are not rare in Great Britain and the U.S.A, and in these latter countries one finds hundreds of large-sized private limited companies changing hands from one set of proprietors or managers to another because the former are unable to provide or find the necessary finance. The managing agency system of finance did not exaggerate financial considerations at the expense of industrial ones any more than any other system of finance.

Next, the charge that owing to the managing agency system of finance, no mill company was able to develop its own system of independent finance, is like arguing in a circle. We have seen already that the managing agency system of finance arose *because of* the fact that there was no system of independent finance. No blame, therefore, should attach to the agents for the fact that independent systems of finance were not developed by the concerns they managed. As a matter of fact, it is *not* true that all concerns managed by managing agents were dependent on them alone for their finance. The concerns managed by European and up-country Indian managing agents were notable exceptions to the general dependence of enterprise in India on managing agency finance.[1]

Finally, the charge that the managing agency system of finance led to enormous speculation in the shares of certain cotton mill companies does not stand the test of scrutiny. It is ture that certain managing agents took an active part in the speculative 'corners' on the Bombay Stock Exchange, but

[1] Memorandum on the Indian Companies' Act (Amendment) Bill, 1936, submitted by the Bengal National Chamber of Commerce to the Government of India.

this had no direct connexion with the *financial* activities of the managing agents in respect of their companies. Even if they had not been the financial guarantors of their companies, they would have indulged in those speculative activities. It is also debatable whether these speculations were the result of the managing agency organization or whether they arose directly out of the fact that most of them were traders first and industrialists afterwards.

Viewed in its proper economic background, the managing agency system of finance was, on the whole, both inexpensive and efficient. This has been recognized in the findings of the various Tariff Boards and of the Central Banking Enquiry Committee of 1929-31, and must be conceded even by the most uncompromising critics of the system. In almost all industries, managing agents found the bulk of the initial capital of a company and provided it with necessary financial accommodation (both direct and indirect) at all stages of its development and particularly during lean years. For this particular service, which is unique in the industrial history of the world, their charges were not excessive, and during the inter-war period of depression many of them advanced money to the companies on the most liberal terms, often ready to forego not only the interest but a substantial portion of the principal as well[1].

For a long time, no accurate figures were available of the part played by managing agency firms in providing finance for industry. Mr. C. D. Deshmukh, the then Finance Minister of India, however, quoted some figures on the occasion of the debate on the Companies Law Bill in 1955. According to him, managing agents had contributed Rs. 29.26 crores to 1,720 companies managed by 1,340 managing agency firms. This worked out at 13.6 per cent of the aggregate paid up capital of these companies. As regards loans and advances made or guaranteed by managing agents, they were of the order of Rs 18.31 crores in a total of Rs 76.45 crores of all kinds of loans and advances, which gave a percentage of 23.95. Although contributing much less than, say, twenty years earlier, managing agents thus provided, even on the

[1] Indian Tariff Board, *Cotton Textile Industry Enquiry*, Vol. I of Evidence and Memoranda, p. 95.

eve of the new Indian Companies Act of 1956, a good proportion of the finance required by industry.[1]

It is also well known that, in periods of crisis, managing agents helped their managed companies liberally with funds. In the 1952 crisis in the tea industry, for example, when banks refused to make advances and many companies could not even pay wages, it was the managing agents who provided the working funds. There have also been cases where managing agents gave up their commission, even the minimum commission of Rs 50,000 provided in the Companies Act of 1956, to enable the companies to sort out their financial difficulties.

The Situation since 1956

The situation does not appear to have altered much even after the new Indian Companies Act came into force in 1956. Partly as a result of the many restrictions placed on the activities of managing agents under this Act and partly as a result of the growth of numerous financial institutions to cater for the varied needs of industry, managing agents are no longer *required* to play a dominant part in providing finance for industry. Nevertheless, such data as are available show that they still continue to function as important intermediaries. Two surveys conducted by the National Council of Applied Economic Research, New Delhi, throw some light on the present situation. The Council found that, in 1958, in the Bombay region, managing agents still contributed 25 to 35 per cent of the total *subscribed* capital of the companies managed by them. In the Calcutta region, the percentage was 17, but this was with reference to the *paid up* capital.

As regards the relative contribution of managing agents in the provision of loans and advances to managed companies, the Council selected two samples of public limited companies. The first included all the 84 largest managed companies, each with a paid up capital of Rs 75 lakhs or more. The second was confined to middle-sized companies, i.e. those with a paid up capital between Rs 10 and Rs 25 lakhs. The former accounted for 41.1 per cent of the paid up capital of all companies so managed and the latter 45 per cent of the

[1] See also D. K. Dutt, *Industrial Management in India,* Calcutta, 1955.

paid up capital. These studies covered the year 1956 and showed that (a) in the case of large-sized companies, more than 70 per cent of the secured bank loans, and, in the case of middle sized companies, more than 50 per cent of such loans were guaranteed by managing agents, (b) even in regard to unsecured loans from banks, 31.5 per cent and 28.4 per cent respectively were guaranteed by them, and (c) direct loans by managing agents formed only a small proportion (1-3 to 7 per cent) of the total working fund. It was significant, however, that even in respect of loans and advances made by the Industrial Finance Corporation of India and the State Financial Corporations, the managing agents concerned had to act as guarantors. And, in Bombay and Ahmedabad, fixed deposits continued to flow in from the public, largely in response to the personal standing and credit of well-known managing agency firms.[1]

A limited enquiry made by the present writer in 1959-60 also reinforces the conclusion that the managing agency system has not outlived its utility in the matter of attracting finance for private industry. The reasons are obvious. Managing agents possess the necessary experience and organisational equipment to perform this function. In fact, the system has a decisive advantage over other institutions in the flexibility of its operations and the standby arrangements that it can provide on account of its close and continuous association with industrial undertakings.

[1] National Council of Applied Economic Research, *The Managing Agency System*, New Delhi, 1959. As the Council has pointed out, a substantial amount of share capital is held *benami* by managing agents. The exact extent of such *benami* holdings cannot be ascertained. The actual share-holdings of managing agents would, therefore, be larger than what has been indicated.

Chapter V

MANAGEMENT BY MANAGING AGENTS

Functions of Managing Agents

Broadly speaking, managing agents in India have performed three important functions. Firstly, they have pioneered new industries, and played the rôle of promoters: they discovered an industrial proposition, assembled the ingredients of the business, and finally procured the funds necessary to put those ingredients into operation. Secondly, they have provided the finance required for industries in respect of both fixed and working capital. Finally, they have performed the day-to-day management of industries—a work that is performed in other countries by a manager or a managing director.

Regarding their work as pioneers and promoters, it is universally acknowledged that they have been more or less instrumental in developing many of the industrial enterprises in India. They brought into existence a means of producing wealth which had not existed before. In due course, however, managing agents were definitely pushed into the background in so far as their pioneering and promoting activities were concerned. This happened for three reasons. Firstly, not every managing agent could claim the ability, experience, or resources of the great business houses by which the system was founded, although every agent, whatever his capacity for fulfilling the functions of managing agents, had benefited by the tradition, and to a large extent owed his existence to it. Secondly, with the progressive industrialization of India, the range of pioneer enterprises became steadily restricted. New enterprises were started on the model of older ones already in existence, and the problem became one more of management and finance than of pioneering. Finally, and this is perhaps most important, very slowly and steadily there grew up a separate class of entrepreneurs who did not always belong to the established 'firms' of managing agents and who, therefore, preferred to do the major work of promotion themselves, although they found it convenient

and useful to consult managing agents or banks.[1]

As to the part played by managing agents as providers or guarantors of finance, we have seen in the previous chapter that but for them many of the industrial enterprises of today would have been non-existent. They bridged important gaps in the financial structure of industry and enabled it to continue its slow but steady career of development.

Finally, we come to the rôle of managing agents as managers of industry. It is this aspect of their work that has been subjected to the bitterest criticism from the public, and it would, therefore, be proper to analyse in detail their duties as managers of industrial enterprises and to consider how far they have abused their position as trustees and managers.

The Dominance of the Managing Agency System

It is interesting to note in this connexion that the system was found to be so 'convenient' by our industrial entrepreneurs that it almost became the 'rule' to entrust the management of companies to firms of managing agents. Sometimes this was entrusted to old and well-established firms, but more often, when new industries were started or new companies were floated, managing agencies were formed by the promoters and their friends and specific 'agreements' were signed between one of these firms and the first Board of Directors even before a company had started functioning. The abnormal hold of the managing agency system on industrial enterprise in this country becomes evident when a comparison is made between the state of affairs prevalent in 1935 and that subsisting in 1955. The percentage of companies managed by managing agency firms increased from 75 in 1935 to over 95 in 1956—a considerable rise, particularly when it is borne in mind that during this period the entire system had come in for a good deal of public criticism.[2]

The Indian managing agency system has been unique, having no counterpart elsewhere. The nearest approach to the system is the Group System of administration in the gold

[1] Memorandum of the Bombay Shareholders' Association on the Indian Companies' Act (Amendment) Bill, 1936.

[2] These percentages have been worked out from the particulars given in the *Investors' India Year Book* for 1935 and 1956 respectively—an authoritative publication by Messrs. Place, Siddons & Gough of Calcutta.

mining industry in South Africa. Of late, however, certain traits of the managing agency system have been introduced in management practices in the U.K. and the U.S.A. In the U.K., in certain categories of industry (e.g. shipping), the companies are managed by 'managers' or 'agents', under managing agreements somewhat similar to managing agency contracts. In the U.S.A., a holding or controlling company becomes interested in a number of concerns, to whom all sorts of technical and financial advice are regularly provided. The key positions in the companies are held on the nomination of the holding company which receives a fee based on gross revenues or net profits, for the various services rendered.[1]

The dominance of managing agents in the sphere of industrial activity in India has been due to certain special circumstances. Firstly, in many industries, the managing agents themselves or their friends held substantial blocks of shares. In the cotton textile industry of Bombay, the percentage of shares held by managing agents was, on an average, 40 to 60 and in exceptional cases it was as high as 90. In the jute mill and coal industries also, managing agents or their friends held an important percentage of shares in the concerns they managed. Secondly, control was secured by managing agents as the principal creditors (or guarantors of credit) of the companies managed. Sometimes managing agents were the largest debenture holders, having charges on the assets and undertakings of the companies. Thirdly, even when managing agents did not hold any substantial percentage of shares in their concerns, they were assured of control because the majority of shareholders, being distributed over long distances, were unable to unite effectively against their dictatorial management. Fourthly, although the managing agency system had been in existence in India for well over a century, the Indian law relating to companies did not curtail their activities until 1936, and consequently many managing agents could do a lot of things without actually transgressing the provisions of the law. Finally, and this is most important, managing agents secured enormous control by means of their written agreements.

[1] George T. Trundle (Ed.), *Managerial Control of Business,* New York, 1954.

Managing Agency Agreements

Managing agency agreements have come in for a good deal of criticism in recent years and hence it is important to analyse what they imply. A managing agency agreement is, strictly speaking, a written agreement between a firm of managing agents on the one hand and an industrial concern (a partnership or a joint-stock company) on the other by which the former undertakes to 'manage' the concern in return for a certain office allowance, with or without some commission on sale, output, or profits.

Until 1936, these agreements were of two kinds—terminable and non-terminable. In Bombay and calcutta a managing agency agreement was usually fixed for a specified initial period, at the end of which the discontinuance of the agreement was dependent on an extraordinary resolution of the company to that effect. The usual period in Bombay was from 30 to 40 years, while in Calcutta it was from 10 to 20 years. The majority required for an extraordinary resolution was invariably three-fourths in Calcutta, while in Bombay it was often as high as four-fifths, and sometimes even five-sixths, including in some cases a provision to the effect that a specified minimum of paid-up share capital should be represented. In Ahmedabad, on the contrary, with hardly any exception, the agreements were subject to no time limit and more or less permanent and non-terminable.[1]

As these managing agency agreements were outside the purview of law until the passing of the Indian Companies' Amendment Act of 1936, they tended to be very arbitrary and autocratic—particularly in Bombay and Ahmedabad. Thus, the Ajit Mills, Ltd., Ahmedabad, started in 1931, appointed agents who were the sole managing agents and were non-changeable, non-removable, and permanent secretaries, treasurers, and agents. The New National Mills, also of Ahmedabad, by their agreement with the managing agents, provided that the appointment of the agents was not liable to be revoked or cancelled on any other ground except their voluntary resignation in writing.[2]

The Act of 1936 introduced certain important changes

[1] Indian Tariff Board, *Report on the Cotton Textile Industry Enquiry*, 1932.
[2] *Ibid.* Vol. II of Evidence and Memoranda.

regulating the managing agency agreements. For the first time, managing agents were brought within the purview of the Act, and a complete set of new sections was introduced, defining their status and also their rights and liabilities. The Act defined a 'managing agent' as 'a person, firm or company entitled to the management of the whole affairs of a company by virtue of an agreement with the latter, and under the control and direction of the directors except to the extent, if any, otherwise provided for in the agreement, and includes any person, firm or company occupying such position by whatever name called.' The special clauses dealing with managing agents were, however, so framed that they did not destroy the system, but continued it with reasonable safeguards.

The very definition of 'managing agents' removed the menace of their usurping all residual powers to themselves: it was no longer possible for them to maintain that they were not subject to the control of the directors. Much more far-reaching, however, were the provisions relating to the duration of appointment, and the duties and liabilities of the managing agent. It was provided that all new appointments of managing agents were to be for a period not exceeding twenty years at a time, and even in the case of existing agencies, notwithstanding the terms of their agreement or any provisions in the Articles, their period of office was to come to an end after twenty years if it did not automatically come to an end earlier within that time. Secondly, it was provided that, notwithstanding anything to the contrary contained in the Articles or the agreement, a company might remove a managing agent if he was convicted of certain criminal offences. Moreover, in general, the appointment, dismissal or variation in the terms of appointment of managing agents was made dependent upon the approval of the shareholders, and it was specifically provided that a change or assignment of his remuneration or any part thereof effected by a managing agent would be void as against the company.

Remuneration of Managing Agents

The managing agency agreement (or 'articles of association'

as it is sometimes called) contained a stipulation regarding payment of a certain office allowance, with or without some commission, by the company to the agents. A good deal of criticism has been levelled at these stipulations on the ground that they were arbitrary, excessive, and unfair. It would, therefore, be proper to consider what these remunerations included and whether industry was justified in making these payments to the managing agents.

Firstly, we may take up the so-called 'office allowance'. In Bombay and Ahmedabad in particular, a certain fixed monthly or annual sum of money was invariably given to managing agents for their head-office expenses. This covered "head office accommodation, rent and taxes thereon, lighting, fans, managing agents' clerical establishment, share of services of despatch, enquiry and cash departments; in several instances, part-time services of a senior accountant and the secretarial staff; and, in several cases, all postages, stationery, telegrams, and menial staff". In Bengal, however, a separate office allowance was not usually insisted upon, unless, of course, the managing agents were compelled to appoint extra or special staff for the individual requirements of a company. Many industrial units, however, made a sort of 'fractional contribution towards the expenses of a federal constitution.'

The second method of payment was by way of certain commission with a stipulated minimum which was payable under all circumstances, whether the industrial companies made profits or not. This had to be paid, without exception, by all concerns under managing agency control. The commission was calculated in one or other of three ways: (*a*) on production, (*b*) on sale or (*c*) on profit. In the early days of the establishment of the cotton mill industry, commission on production (or output) was the vogue, The system, however, led to over-production and sacrifice of quality to quantity, as managing agents were always tempted to increase the volume of output in order to make higher profits. It was, therefore, largely abandoned towards the close of the nineteenth century, and the system of commission on profits was adopted. 'Of the 71 mills which were members of the Bombay Millowners' Association in 1928, only one mill paid commission

on production; one mill was managed by a managing director whose remuneration was fixed by the Board of Directors; 8 mills paid commission on sales, and 61 mills paid commission on profits.' The rate was usually 10 per cent on profits. In Ahmedabad, however, the commission was calculated on gross proceeds of sales and the rate varied from 3 to 4 per cent. In the other industrial centres of the cotton industry, the most common method was that of a commission on output, but there were a fair number which paid commission on sales and a few which calculated it on profits. In the jute industry, the majority of the mills paid commission on sales, but there were a few which paid commission on profits besides a minimum commission and a generous allowance for office expenses. The same was the practice in the coal industry. A commission of 7½ per cent on profits was the usual remuneration for managing agents engaged in the sugar industry, although, in the case of several companies, floated after protection was granted, provision had been made for commission on sales, and in some cases for a combined commission on sales and profits.[1]

Of the three systems in vogue, there is no doubt that the system of commission on profits was the best. 'The great defect of the system of commission on production was that it tended to concentrate attention on output rather than on quality, but a greater objection to that system was that it removed the incentive to the disposal of production at the best possible price. These same objections applied, though to a lesser degree, to the system of commission on sales. The mills which adopted this system, unless they were managed by agents who held the majority of the shares, were naturally concerned only with getting rid of their production and not with the price at which it was disposed of.' Moreover, where the managing agent was paid on production or sales, his interest became divorced from that of the shareholders by making him reluctant to agree to short-time working even though it might be necessary in the interest of the industry as a whole: he became interested primarily in the output of his own concern and hardly cared to consider the far-reaching

[1] Memorandum of the Bombay Shareholders' Association on the Indian Companies' Act (Amendment) Bill, 1936.

consequences of excessive output in the profit-making capacity of the entire industry.

Critics of the managing agency system contended that the remunerations drawn by the managing agents were arbitrary and excessive. Apologists of the system, however, retorted that a managing director would have charged as much, if not more. 'Managing agents manage as well as finance, whereas managing directors would manage but not finance, and hence industry should be prepared to pay slightly more to the managing agents.' There are, however, three important points to be considered Firstly, for the direct services that managing agents performed in respect of finnance, they always got a separate remuneration (viz. interest) and they should not have been anxious to get something 'extra' for the indirect services they performed by way of securing loans from others or by guaranteeing the loans. Secondly, while a new or difficult enterprise should always be prepared to pay more for management, the burden of payment should have been gradually scaled down, as experience was gained and as industry became well established. Thirdly and finally, the main objection of critics was not so much to the office allowances and regular commissions paid, but to certain arbitrary devices that were sometimes adopted to get additional or secret profits or both. It is to these that we should now turn.

The first device consisted in calculating the managing agent's remuneration on profits before depreciation was set aside. Not only this : very often, in calculating the percentage, interest on loans and advances, profits by way of premium on shares sold, profits on sale, proceeds of forfeited shares, or profits from the sale of the whole or part of the undertaking in the company, were not excluded from gross profits, with the result that the managing agents were able to bite off a much larger share of the cake than they should. To quote some instances : in 1921, the Simplex Mills Co., Ltd., earned a premium of over Rs 10 lakhs on the issue of additional capital, and the managing agents charged commission on this; again, in 1935, the Tata Power Co., Ltd., issued to its shareholders as well as sold in the open market certain shares which had been previously forfeited for non-payment of calls, and earned a large amount of premium on the sale of these

shares, the managing agents charging their commission on the premium so earned.[1]

It has been contended by some apologists of this method of calculating commission on profits that it did not by itself adversely affect the financial position of the industrial company, because (so the argument ran) if depreciation and other elements were deducted, the scale of commission which was normally 10 per cent would have increased and the net cost to the company would have remained more or less the same. This does not, however, seem to be correct. Firstly, many companies charged less than 10 per cent commission even after allowing for depreciation, and it could not, therefore, be argued that a rate round about 10 per cent on gross profits was, so to speak, the absolute minimum. Secondly, any attempt to increase the rate to more than 10 per cent (when commission was calculated after making certain deductions) would have been resisted, because a rate like 15 or 20 per cent would, on the very face of it, have seemed excessive and exorbitant.

The second device to get an additional remuneration for managing agents was by the method of compensation. If the business of a company was transferred during the pendency of the agreement to another party, the managing agent had the right of continuing in office in spite of the change of ownership; in case of refusal, he was entitled to claim compensation. In Bombay, when a company was wound up, the managing agent was entitled to claim compensation, according to the general practice, on a scale equivalent to the commission earned by him during the previous five years, and, in individual cases, even a higher rate of compensation was claimed. At Ahmedabad, the general practice was to claim compensation at a rate ranging from five to seven times the average annual commission earned by the managing agent over a period of five years. In the latter place, sometimes the managing agent was entitled to compensation even if the agency had been terminated by mutual agreement. On the other hand, in Calcutta, there were no agreements containing a provision for the payment of compensation as in Bombay and Ahmedabad. Even in those few cases

[1] *ibid.*

where provision existed for compensation, it was expressly provided that such compensation would be payable only if the winding up took place at the instance of a party other than a creditor, and the amount payable would be mutually agreed upon, failing which it might be settled by arbitration.

A third device to get additional remuneration was by inserting clauses in the agreement for supplementary or secret profits. In one managing agency agreement there was a reference to 'every profit, remuneration, and compensation including any profit which they (the managing agents) might make as the agents for the insurers of the properties, assets, and effects of the company, and any profit which they might make under any arrangement with the agents of the company for selling cloth, yarn or muccadams of the company.' The latter class of profits clearly pointed to the fact that there was an arrangement for some additional (and secret) profits in addition to the usual office allowance and commission.

All these show that although the normal office allowance and commission payable to managing agents were not excessive, the special devices resorted to by some managing agents to get more out of a company were both unfair and excessive. The managing agency system came into disrepute mainly because it had given opportunities to some unscrupulous (and dishonest) persons to get various kinds of extra remuneration without actually transgressing the law relating to companies.

The Act of 1936 sought to tackle the above question of remuneration. It laid down that no managing agent, appointed after the amending Act came into force, could stipulate for his remuneration anything other than a percentage of the net profits of the company, with a provision for minimum remuneration in the case of inadequacy or absence of profits, together with an office allowance. Any other form of remuneration had to be specially sanctioned by the shareholders. The mode of ascertaining the net profits was also laid down in detail and a list of deductions (e. g. the usual working charges, interest on loans and advances, repairs and outgoings, depreciation, bounties or subsidies received from the Government or a public body, profits by way of

premium on shares sold, etc.) enforced a reasonable basis for the calculation of profits.

Assignment of Function and Interests by Managing Agents

Another abuse that had crept into the managing agency system was the practice of assignment of functions and interests. In Bombay and Ahmedabad, the agreements generally provided that the managing agent might assign to a third party his interests or his duties under the agreement, and for this assignment no specific sanction of the directors was required. The Indian Tariff Board came across a case in 1932 in which the managing agent could assign not merely his interest in the profit of the company, but the agreement itself, to a third party. This agreement was executed by one of the most important managing agency houses of Bombay. To quote some specific instances : Messrs. Currimbhoy Ebrahim & Sons, Ltd., mortgaged their agency commissions in several companies under their control, and, as a result the mortgagee acquired considerable influence in the management of the affairs of those companies; again, the partners of Messrs. Morarjee Goculdas & Co. mortgaged their commission in the Sholapur and Morarjee mills with the result that the mortgagees acquired undue influence over those mills. Similarly, in Ahmedabad, it was not unusual in agreements to provide for the right of the managing agent to assign at will not merely his interest in earnings but also the whole agreement. A usual feature of the system in Ahmedabad was that the right to the commission earned by the managing agent was divided among several persons holding fractional shares, these persons generally being those who had helped the managing agent in the promotion and financing of the company in the early stages. Even in Calcutta, where such sweeping rights of assignment without the sanction of the company were unknown, there were certain types of agreement in which the powers conferred on the managing agents could be vested in their assigns as well as successors.

This system of assignment was open to objection for two main reasons. Firstly, as a result of these assignments, companies became subject to undesirable outside influence, and shareholders became all the more powerless to exercise any

check on these outsiders. Secondly, the *raison d'être* of the managing agency system was the financial standing of the managing agent behind his company. If, therefore, the managing agent was reduced to a financial state where he had to mortgage his commission, the credit of the company suffered irretrievably.

Inter-investment of Funds by Managing Agents

Another feature of the managing agency system was the practice of inter-investment of funds among companies under the same agents. This was prevalent in the cotton textile industry of Bombay and Ahmedabad, but it was not confined to that industry alone. Almost all industries managed by managing agents shared this feature.

Inter-investment took two forms: surplus funds raised on the credit of one company would be invested in other companies under the same managing agent, or debentures issued by one company would be subscribed to entirely or mainly by other companies in the same group or in companies in which the managing agent had an interest. Now, when everything went well, this inter-investment did not cause any particular harm to any of the enterprises. On the one hand, the comparatively weak concerns profited by this inter-investment; on the other, the comparatively strong ones were satisfied, because their funds were quickly invested and were at the same time (especially when it was a cash investment) easily realizable. But over a long period, this practice had definite drawbacks. What really happened was that, although the financial position of an individual company was strong, its shareholders were often deprived of its benefit by being called upon to assist weaker sister concerns which were managed by the same managing agent. Not only did it involve serious unfairness to shareholders of the concern whose funds were thus transferred, but the practice often led to the perpetuation of thoroughly insolvent concerns which it would have been to the interest of the industry as a whole to have closed down.

Loans to Managing Agents

Another far-reaching abuse of the system was the practice

of managing agents taking huge loans or advances from the companies they managed. The allegation that many managing agents took such loans or advances was hotly denied by the Bombay and Ahmedabad Millowners' Associations before the Indian Tariff Board Cotton Textile Industry Enquiry of 1932, but the Bombay Shareholders' Association proved in 1935, with the help of facts and figures, that the evil existed. Nor was this evil confined to the cotton textile industry. The loans taken by Messrs. Vakil Ankleseria & Co. from the Western India Oil Distributing Co., Ltd., brought infinite trouble upon the company which was eventually saved only by reorganization. The loans obtained by Messrs. J. F. Madan & Co. from the Madan Theatres, Ltd., tell a similar tale. The function of managing agents is to finance companies. To allow companies to finance managing agents is, to say the least, fundamentally wrong. Such abuses of the system have had far-reaching consequences. Apart from inflicting heavy losses on individual companies, their shareholders, and their creditors, the general confidence of investors in the integrity of managing agents was rudely shaken by these questionable methods of 'management'.

Restrictions imposed by the Indian Companies (Amendment) Act of 1936

Besides prescribing the duration of managing agency agreements and specifying the duties and liabilities and remuneration of managing agents, the Indian Companies (Amendment) Act of 1936 absolutely prohibited the practice of giving or guaranteeing loans to such agents. The inter-investment of funds by managing agents when they had several companies under the same management was also forbidden. Similarly, the employment of the funds of a company in the purchase of the shares and debentures of another company under the management of the same managing agent was prohibited. Managing agents were also prevented from carrying on, on their own account, business which was of the same nature as, and directly competed with, the business of the managed company. Finally, the practice of managing agents packing the Board of Directors with their own nominees was rendered difficult by a Section directing that no managing agent should

be allowed to nominate more than one-third of the total number of directors.

These and other extensive changes introduced by the Amendment Act of 1936 were assailed by certain sections of business men at that time as having violated the fundamental principle of the sanctity of contract. It was asserted that existing contracts were being interfered with and a company was being prevented from choosing the form of management, and also the basis of remuneration, which it considered to be the best in its own interests. It was even stated that 'undue legislative restrictions like those embodied in the Act would kill a system which had rendered such splendid service to industry in the past.'[1] It was also suggested that limiting the period of managing agency to twenty years was quite inadequate, in view of the fact that industrialization in India was still in a nascent state. 'It takes about ten to fifteen years for any industry to be established on a profitable and economic basis, and it would not, therefore, be sufficient inducement to the managing agents to develop an industry if they are to relinquish the fruits of labour so soon after they have succeeded in developing it. . . . Further, the restrictive clauses, by dissuading managing agents from embarking on new industrial ventures, would only retard the industrial development of the country.'[2]

These gloomy prophecies did not, however, materialise. As we have seen already, even after 1936, not only was there no relaxation of the grip of the managing agency system over private industrial enterprise in this country, but there was a further extension of it. It is true that certain glaring malpractices which were rampant before 1936 were prevented, but business acumen soon got to work and was able to find ways and means of circumventing the legal restrictions imposed. In not a few instances, many managing agency firms sought the assistance of lawyers and other experts versed in company law and, with their help, devised ways and means of keeping within the letter of the law and at the same time

[1] Circular letter No. 193|1936 of 20 June 1936, from the Bengal Chamber of Commerce, Calcutta, on the Indian Companies' Act (Amendment) Bill, 1936.

[2] Memorandum of the Federation of Indian Chambers of Commerce and Industry on the Companies' Act (Amendment) Bill, 1936.

continued their undesirable practices in a disguised form.[1]

The continuance of this unsatisfactory state of affairs was facilitated by the unpreparedness or ineffectiveness of the procedure in administering the Act as it stood. Notwithstanding the amendments made in 1936, the Indian Companies Act had a number of loopholes which became evident only as the years passed. 'Large changes had taken place in the organisation and working of joint-stock companies, and, over a wide sector that was dominated by new elements in trade and industry the character of company management had also materially altered. In many cases, conventional methods of company management were discarded in favour of less orthodox and more venturesome techniques, which the existing company law was unable to control adequately.' But much more serious than the obvious loopholes was the inadequate and perfunctory manner in which the Act was administered. The Company Law Committee had to admit that the Indian Companies Act was perhaps the most under-administered of all the Central Acts relating to trade and industry.

This was due to a number of facts. Firstly, although the legislative and executive authority in respect of the regulation and inspection of joint-stock companies vested in the Central Government, in practice the Central Government had very little to do with the administration of the Companies Act. They were content to delegate all their functions under the Act, except a few, to the Governments of the Provinces (later, States). The powers thus delegated were so extensive that, for all practical purposes, the responsibility for the administration of the Act had rested with the State Governments, as if the Indian Companies Act were an Act of the State legislatures and not of the Indian Parliament.[2] The reasons for such delegation were partly historical, partly

[1] Some firms paid fabulous fees to lawyers and experts for this service, while others maintained a separate section, ostensibly to comply with the provisions of the Companies Act, but really to find ways and means of circumventing them. The author himself was informed by some of his lawyer friends how very much their services were being sought by managing agency firms mainly with a view to helping the latter to remain law-abiding and at the same time continue all the 'advantages' previously enjoyed.

[2] For a statement showing the nature and extent of the powers delegated, see *Report of the Company Law Committee*, New Delhi, 1952.

constitutional and partly financial. The doctrine that Government must concern itself with the general state of the economic health of the country became familiar only after India attained her independence. As a result, 'the full social implications of Company law were hardly realised and the administration of the Act was regarded primarily as the negative function of preventing the Joint-Stock Companies from contravening the statutory requirements. This negative function could be performed as easily by the Provincial Governments as by the Central Government.'

Secondly, on the plea of observing 'economy' in administration, the power to appoint Registrars of Joint-Stock Companies was delegated to the Provincial (State) Governments. They, however, took very little interest in the administration of Company law and the position in 1952 was that, barring Bombay and West Bengal, none of the States had any full-time Registrars, although the number of joint-stock companies at work in India had exceeded the figure of 22,000 since 1947. In all other States, the Registrar's duties were 'performed' by officers of the State Government in addition to their other duties. No wonder that the total budget in respect of the establishments of the Registrars of Joint-Stock Companies in *all* the States never exceeded Rs 5 lakhs per annum!

The cry for Company law reform, therefore, gathered momentum from about 1947 onwards. Having obtained freedom, the attention of the leaders and those in authority was turned towards the need for reform: the organization and management of joint-stock companies could no longer be left at the point at which it stood in 1936.

Chapter VI

THE NEW INDIAN COMPANIES ACT AND ITS ECONOMIC SIGNIFICANCE

An Historical Retrospect

Following the English Companies Act of 1844, an Act for 'the registration of joint-stock companies' was, for the first time, enacted in India in 1850. Under this Act 'every unincorporated company of partners associated under a deed containing a provision that the shares in the stock or business of the said company were transferable without the consent of all the partners, and also every company established for some literary, scientific or charitable purpose, which did not carry on any business for the pecuniary benefit of any of the proprietors or shareholders' became entitled to registration, and the Supreme Courts of Calcutta, Madras and Bombay were authorised to order such registration. The privilege of limited liability was not, however, conferred on the members of such companies.

Another Act was passed in 1857 'for the incorporation and regulation of joint-stock companies and other associations, either with or without limited liability of the members', but, under this Act, the privilege of limited liability was not extended to any company formed for the purpose of banking or insurance. This latter disability was removed by an Act passed in 1860.

It was not until 1866, however, that a comprehensive Act was passed[1] affirming the principle that 'no member of a joint-stock association shall be liable for more than the unpaid portion of his share, and that, in the case of guaranteed companies, no member shall be liable beyond the amount of his guarantee.' This Act was recast in 1882[2] embodying the amendments that had been incorporated in the company law in England up to that time.

Between the years 1882 and 1913, five amending Acts[3]

[1] Act X of 1866.
[2] Act VI of 1882.
[3] Act VII of 1887, Act XII of 1891, Act XII of 1895, Act IV of 1900 and Act IV of 1910.

were passed in India, but these related to minor amendments only. Finally, in 1913, a comprehensive Act was passed,[1] following the English Companies (Consolidation) Act of 1908. Some minor amendments were made later in the Indian Act between 1914 and 1932.

By this time the situation had become ripe for a thorough overhaul of company legislation. Firstly, the Act of 1913 and the subsequent amending Acts had not taken into account a system which was in vogue in India, but unknown in England, viz. company management through managing agents. Indian company law had followed the English law rather too closely and remained conveniently silent about this important economic institution in India. The result was that unscrupulous persons had begun to take advanage of the loopholes and omissions in the law, and abuses and malpractices by some managing agents had become far too common a phenomenon. Secondly, while in England some modifications had been made in the law in the light of experience, no corresponding steps were taken in India. In 1926, a Committee presided over by Mr. Greene, K.C., examined the existing law and made extensive recommendations, and many of these were subsequently incorporated, with or without modification, in the Companies' Consolidation Act, 1929. India, however, continued to labour under the antiquated Act of 1913 (as amended in a few particulars between 1914 and 1932). Finally, no serious attempts were being made to study the Indian company law from a comparative standpoint—in the light of the experience of the working of joint-stock associations in other countries. In 1908 and again in 1911, analyses of the company laws of the United kingdom, India, Canada, Australia, New Zealand and South Africa were made in England by direction of the Board of Trade,[2] but no serious effort was made to secure uniformity of the company laws of the Empire, nor did India ever seek to amend her laws in the light of the working of the company law in other parts of the Empire.

Agitation for removing the defects of the Indian Act

[1] Act VII of 1913.
[2] *Comparative Analyses of the Company Law of the United Kingdom, India and the Dominions*, 1911 (Cmd. 5864), p. 6.

continued ceaselessly after 1930, and at last in September 1934 the Government of India placed a lawyer[1] with experience in the administration of company law on special duty to examine the materials collected and to make proposals for the amendment of the Indian law. This lawyer's report was published in January 1935, and his propcsals were further discussed by a small committee of business experts specially convened for the purpose. In this committee representatives of diverse interests—Chambers of Commerce, Shareholders' Associations, Millowners' Associations, and the Impeerial Bank of India—took part and made their suggestions. Out of these proposals and discussions there crystallized a Bill to amend the Indian Companies' Act of 1913 and this was introduced into the Indian Legislative Assembly by the Law Member, the Honourable Sir N. N. Sircar, in March 1936. The Bill was considered by a very representative Select Committee and came back to the Assembly with a number of important modifications in August 1936. After this, the progress of the Bill was rapid: there was an exhaustive discussion on almost every clause of the Bill on the floor of the Assembly, but the Honourable Member-in-charge piloted it so very skilfully that it emerged from the Assembly and received the assent of the Viceroy before the end of the year.[2]

The revision of the law in England in 1929 took the form of a consolidating Act which completely replaced the Act of 1908. In India, however, the form of the Act of 1913 was retained and the changes, extensive though they were, were introduced in the form of amendments.[3] In the amendments, the pattern followed in the overhaul of the English law was adopted where the problems dealt with were problems common to India and England. There were, however, some special clauses —for the first time—for problems peculiar to India herself, for example, those connected with the managing agency system.

As was well put by Sir N. N. Sircar in the Indian Legislative Assembly, the new Act[4] was based on two considerations:

[1] Mr. S. C. Sen, a solicitor of Calcutta.

[2] The Act came into operation on 15 January 1937.

[3] This was done because there were 'manifest advantages in retaining the form of the existing Indian Act with the administration of which the courts were familiar.'

[4] The new Act dealt with six different problems: (a) mushroom and fraudulent companies; (b) provisions relating to the issue and contents of prospectuses;

firstly, that every attempt should be made to make extremely difficult the malpractices which had come to light as a result of the working of the Act of 1913; secondly, that the provisions for stopping these apprehended malpractices must not be so unreasonable and onerous as to keep away honest men from having anything to do with joint-stock companies. As a matter of fact, the new Act attempted to arrive at a mean between two extreme views—one view which is difficult to shake off from one's mind, viz. that business men or, for that matter, any set of men, can be made honest by force of statute, and that all possible avenues of dishonesty and malpractice can be effectively stopped by legislation, and the other view that nothing can be done thereby and hence things should be allowed to run their usual course. The new Act recognized that the management must have some freedom in pursuing its policy, and that it would be unwise to lose all sense of proportion about the abuses in which, after all, only some companies had indulged; it also emphasised that no legislation, howsoever comprehensive, could possibly rouse those shareholders who had made up their minds to slumber.

Between 1936 and 1955, there were further periodical amendments of the Act, necessitated by the defects disclosed in the Act and also by the constitutional changes introduced by the Government of India Act, 1935. Some further formal amendments had to be made when India attained her independence and, later, when, in 1950, the constitutional status of India was changed into that of a Sovereign Democratic Republic.

These amendments did not, however, meet the situation adequately. Several lacunae in the Act of 1913 (as amended by the Act of 1936) and the defects in its administration 'had enabled some business men and financiers, with no long and honourable traditions of service to the community, to misuse and sometimes to pervert the provisions of the company law to serve their private ends, while the absence of any adequate and effective organisation for the administration of the Act, rendered remedial action extremely difficult. As long as the

(*c*) increased disclosure to shareholders of the financial position of companies and increased rights of shareholders in connexion with the management of companies; (*d*) managing agents; (*e*) provisions applicable to winding up; and (*f*) special provisions to govern banking companies.

war lasted, the expansive pull exerted by the war economy on domestic production masked these malpractices, but the end of the war brought them to the surface and exposed them to the full view of an increasingly critical public, which had been already hit hard by the aftermath of the war, and was thereafter apt to ascribe most of its post-war ills to these undesirable practices in trade and industry.' As a matter of fact, several Commissions and Committees (e.g. the Fiscal Commission, the Income-tax Investigation Commission and the Planning Commission) had drawn pointed attention to some of these practices. A demand for early reform of the company law was, therefore, reiterated by the shareholders as well as the general public.

Meanwhile, a comprehensive enquiry into the working of the company law had been made in the U.K. and other Commonwealth countries. Towards the end of World War II, i.e. in 1943, a Company Law Amendment Committee, more familiarly known as the Cohen Committee, was set up in the fomer country with Lord Justice Lionel Cohen as Chairman. This Committee submitted a most comprehensive report after a laborious enquiry spread over two years. In South Africa, a Commission, known as the Millin Commission, also went into the question of company law reform in that country and made some important recommendations. Similar enquiries were initiated in Canada, Australia and the U.S.A.

As a first step, the Government of India appointed in 1946 Mr. Tricamdas Dwarkadas, as an officer on special duty, to indicate fully the lines on which the Indian Companies Act should be revised, not only in view of the amended provision of the English Companies Act, but also in the light of the development in trade and industry since 1936. Between 1946 and 1947, Mr. Dwarkadas submitted his recommendations in three parts, but was unable to complete his assignment on account of his other preoccupations. The Government of India thereupon appointed Mr. V. T. Thiruvenkatachari, Advocate General of Madras, to carry out some further studies in the matter and advise Government. Mr Thiruvenkatachari completed his task in October 1948.

The reports of Messrs. Dwarkadas and Thiruvenkatachari

were subjected to a detailed departmental scrutiny in the old Ministry of Commerce.[1] The proposals formulated as a result of this scrutiny were embodied in a 'Memorandum on the Amendment of the Indian Companies Act' and circulated to all State Governments and organised industrial and commercial bodies in December 1949. Comments and observations were received during a period of over six months in 1950, running into many hundreds of pages of printed matter.

Thereupon in October 1950, the Government of India set up a Committee (popularly known as the Company Law Committee) with Mr. C. H. Bhabha, a former Commerce Minister of the Government of India and a prominent businessman, as Chairman, 'to consider and report what amendments were necessary in the Indian Companies Act, 1913, as amended by Act XXII of 1936, with particular reference to (*a*) the formation of companies and day-to-day conduct of their business, (*b*) the powers of the management *vis-à-vis* shareholders, and the relations between them, (*c*) the safeguards required against abuse of such company practices as the interlocking of directorates, voting control by majority interests in company ownership and management, etc., which might be prejudicial to the public interest, and (*d*) the measures necessary to promote efficient and economic management of companies.' The Committee submitted its report to Government on February 29, 1952. This report was very comprehensive in character: it not merely analysed the growth of companies and company law in India, but also made various recommendations in regard to the (*a*) constitution and incorporation of companies, (*b*) shares and share capital, (*c*) company meetings and proceedings, (*d*) management of companies—by managing agents as well as managing directors or managers, (*e*) accounts and audit, (*f*) inspection and investigation and (*g*) winding up of companies. Finally, it recommended the setting up of a Central Authority to direct and supervise the administration of the Indian Companies Act.

The Company Law Committee stated that if Government accepted their recommendations, these should form the basis

[1] Mr. N. K. Majumdar, a former Registrar of Joint-Stock Companies, West Bengal, was placed in charge of this work.

of a consolidating measure and not merely of an amending Bill. Accordingly, they annexed to the Report an addendum attempting redrafts of several sections of the Indian Companies Act and also drafts of some new sections, based on analogous provisions of the English Companies Act.[1]

Government lost no time in acting on the Report. The Member-Secretary of the Committee was placed on special duty to give practical shape to the recommendations in the form of a Bill, but the actual draft could not be made ready until the middle of 1953, as differences of opinion arose between different sections of the Congress Parliamentary Party as to the extent to which some of the restrictive and penal provisions (particularly those relating to managing agents) should be incorporated in the Bill.[2] There were some who felt that the recommendations of the Committee did not go far enough and they insisted on certain additional provisions being included. Eventually, a compromise was reached, and the Companies' Bill, 1953, was introduced in the Lok Sabha (lower house of the Indian Parliament) on 2 September of that year.[3] After some general discussions, the Bill was referred to a Joint Committee of both the houses in May 1954. The Committee held 61 sittings in all, made important changes in the original Bill and submitted its report on 2 May 1955.[4]

Discussions in the Joint Committee were prolonged, often revealing a wide divergence of views. As a matter of fact, out of 49 members of the Joint Committee, as many as 14 submitted separate notes or minutes of dissent. The Bill was, therefore, hotly debated in the legislature and some members wanted further 'improvements' to be made in the Bill as amended by the Select Committee. At a certain stage, the

[1] For the materials incorporated in this section, the author has drawn freely on the Report of the Company Law Committee.

[2] It is interesting to recall that one of the members of the thirteen-member Committee (Mr. Mohanlal L. Shah—later, Minister of State in the Ministry of Finance in the Central Government) submitted a note of dissent on some points, particularly on the sections relating to managing agents. He felt that some of the changes recommended by the Committee 'had overstepped the practical necessities and requirements of the situation.' (p. 213 of the Company Law Committee Report).

[3] Bill No. 46B of 1953. It was a Bill of formidable size, running into 612 clauses and 12 schedules. It was the longest Bill ever presented to the Indian Parliament.

[4] When it emerged from that Joint Committee, the Bill had 649 clauses and 12 schedules. The final Act consists of 658 clauses and 12 schedules.

Finance Minister (Mr. C. D. Deshmukh), who was piloting the Bill, threatened to resign if the Bill, as amended by the Joint Committee, were not accepted by the legislature substantially without modification. Tempers, however, soon cooled down and, after the debate on the controversial clauses was over, the Bill was passed by both houses without much difficulty. The Bill received the assent of the President early in 1956 and came into force on 1 April of that year.

Considerations behind the New Act: Primacy of Social Interests

Unlike the earlier Act of 1936, the Act of 1956 had a broad social objective which transcended such limited objectives as stoppage of malpractices or protection of the interests of shareholders. The activities of joint-stock companies affect not merely the shareholders but also the general public as the consumer of the goods and services produced by them. Hence, the protection of 'social interests' had to be superimposed over the rights and privileges of other parties directly interested: private industrial enterprise, as organised under joint-stock companies, had to be fitted into the general pattern of State policy, which had undergone radical changes since 1936. An important directive principle of this policy, as embodied in the Constitution of India, was that 'the State shall so direct its policies that the operation of the economic system does not result in the concentration of wealth and means of production to the common detriment.' The changes made in the Bill in the Joint Select Committee stage were in recognition and furtherance of this principle.

Nevertheless, as was emphasised by Mr. C. D. Deshmukh himself, company law is primarily concerned with means and not ends. 'It attempts to provide a legal framework for the corporate form of business management in which organisation, capital and labour are brought together in a particular form of relationship which constitutes the essence of private enterprise. While it should be subject to the acceptance of some broad social objectives and of some recognised standards of behaviour, the basic problem of company law is to consider to what extent it is possible to adjust the structure and methods of the corporate form of business management with a view to weaving an integrated

pattern of relationship as between promoters, investors and managements.'[1]

According to Mr. C. D. Deshmukh, the new Act sought to secure the following: (*a*) the efficiency of corporate business should be increased; (*b*) managerial efficiency should be reconciled with the legitimate rights of investors; (*c*) the interests of creditors and other partners in production and distribution should be duly safeguarded; and (*d*) the attainment of the ultimate ends of social policy, including labour relations, should be helped and not hindered by the manner in which the corporate form of business is conducted. This balancing of private and social interests is not an easy task in any country. In India, it was rendered more difficult by the complicated nexus of relationship which had been built up over the years between the promoters, the investors and the management of a company.

In the light of the above facts and circumstances, we shall now try to assess the economic significance of the changes introduced by the new Act in so far as they have a direct bearing on industrial enterprise in this country.

Managing Agents and Restrictions on their Powers under the New Act

As we have noticed already, the most important (and the most controversial) portion of the Act was that dealing with managing agents. The very first clause in this part stated that the Central Government might, by notification in the official gazette, declare that, as from a specified date, all companies in certain classes or types of industry or business, shall cease to be managed by managing agents at the end of three years from the specified date or on 15 August 1960, whichever was later. A second clause said that, after the commencement of the Act, a managing agency company should not be managed by another managing agent. In all other cases, the appointment or re-appointment of managing agents by a company must be approved first by the company itself at a general meeting and then by the Central Government. Even here, Government could withhold its approval until it was satisfied that (*a*) it was not against the public

[1] *Lok Sabha Debates*, Vol. IV, No. 55, speech of Mr. C. D. Deshmukh on 28 April 1954.

interest to allow the company to have a managing agent and (*b*) the managing agent proposed was, in its opinion, a fit and proper person to be appointed or re-appointed as such and the conditions of the managing agency agreement proposed were fair and reasonable. Then there were the further provisions that (*a*) after the commencement of the Act, when a managing agent was appointed for the first time it should not be for a period of more than 15 years and (*b*) in cases of re-appointment, it should not be for a period of more than 10 years at a time.

Restrictions were also imposed on the number of companies on which a person could serve as a managing agent : after 15 August 1960, no person was to hold office at the same time as managing agent in more than ten companies. As regards existing managing agents, it was stipulated that the term of every managing agent should terminate on 15 August 1960, unless he was re-appointed for a fresh term before that date *in accordance with the provisions of the Act.* There were also provisions for automatic vacation of office by a managing agent if he was adjudged insolvent or had been convicted for any offence and sentenced to imprisonment for a period of not less than six months. In cases of fraud or breach of trust, or of gross negligence and mismanagement, a managing agent might be removed from his office by a resolution of the managed company. Finally, it was laid down that a transfer of his office by the managing agent should not take effect unless it had been approved both by the company and by the Central Government and that, after the commencement of the Act, managing agencies should not be heritable.

As regards remuneration, the Act said that a managing agent should not ordinarily be paid, by way of remuneration, any sum in excess of 10 per cent of the annual net profits of the managed company and that additional remuneration could be paid only if such payment had been sanctioned by a special resolution of the company and been approved by the Central Government as being in the public interest.[1]

The Act also placed restrictions on the powers of managing agents. The managing agent of a company was to

[1] The Act also laid down in detail how 'net profits' were to be calculated for this purpose.

exercise his powers subject to the superintendence, control and direction of its Board of Directors and subject also to the provisions of the memorandum and articles of the company. Restrictions were also placed on (*a*) the grant of loans to managing agents by the managed company, (*b*) the grant of inter-company loans under the management of the same agency firm, (*c*) purchase by a company of shares etc. of other companies in the same group, (*d*) engagement by a managing agent in business competing with the business of the managed company, and severe penalties have been prescribed for contravention thereof.[1] Finally, further restrictions were imposed on the right of the managing agent to appoint directors : he would now be able to appoint not more than two directors where the total number of directors exceeds five, and not more than one director where the total number does not exceed five.

These various restrictions were assailed by some as extremely harsh, by others as grossly inadequate. The former school of thought was represented by business men and industrialists and also by a section of economists: the latter by the more radical parties and by another section of economists. Let us examine, as objectively as possible, the arguments put forward by these two schools of thought.

As was pointed out by the former, the Act went far beyond the original recommendations of the Company Law Committee. That Committee had given the matter very careful thought from every conceivable angle and had definitely stated that 'under the present economic structure of the country, it would be an advantage to continue to rely on the managing agency system....Shorn of the abuses and malpractices which have disfigured its working in the recent past, the system may yet prove to be a potent instrument for tapping the springs of private enterprise.' The Act, however, while not openly and expressly abolishing the system, introduced provisions of a sweeping character which might 'lead to its virtual abolition'. 'The psychological effect of these provisions would prove to be far more disastrous to

[1] Some of these restrictions were already in existence in the Amendment Act of 1936, but they were further tightened up in the Act of 1956.

the economy than the physical effect of the provisions.'[1] 'The Act bears the mark of the preconceived ideas of certain powerful political elements obsessed with the idea of gradually abolishing the system, but the problem which it has failed to solve is that of an alternative form of managerial organisation to replace the managing agents. That the system is indispensable in the present circumstances is proved by the fact that it has been found necessary to allow in notified industries the appointment of 'Secretaries and Treasurers', whose functions, powers and terms of appointment differ only slightly from those of managing agents....It is not advisable to place needless restrictions on the working of *all* joint-stock companies because of the malpractices of *a few*. ....If the Government are in favour of abolishing the managing agency system, they should try to foster some alternative system of management.'[2]

To these arguments, the reply of those who thought that the provisions of the Act did not go far enough (in so far as managing agencies are concerned) was that 'the capital market was much more developed and it would not, therefore, be difficult to raise capital from the market in the absence of the managing agency system.' Why then give a lease of life to a system which was a relic of industrial feudalism in the country and already stood self-condemned?[3] As regards the argument that the Act had gone much further than the Company Law Committee had recommended, and for no obvious reasons, the reply was that 'certain significant and quite large-scale developments in the sphere of industrial management of finance had taken place since 1952, brought about by the impact of planning and the entry of the State in an active role initiating and sponsoring industrial development, and these had rendered the earlier conclusions of the Company Law Committee quite out of date.' As such, they argued, not only were the restrictive provisions not onerous, but positively half-hearted and weak!

[1] Observations made by Mr. N. C. Karayalar on the Report of the Joint Committee on the Companies Bill.

[2] Note of dissent by Messrs. Tulsidas Kilachand and G. D. Somani on the Report of the Joint Committee on the Companies Bill.

[3] Note of dissent by Messrs. M. S. Gurupadaswamy, V. K. Dhage, B. C. Ghose and Amjad Ali on the Report of the Joint Committee on the Companies

The Managing Agency System Today

After five years of working of the Act, it is now possible to say that, despite all restrictions and regulations, the managing agency system has 'managed' to survive. In all fairness to the framers of the Act, it must be stated, however, that they never intended to 'end' the system: they merely wanted that it should function under proper control and regulation by the Government.[1]

Let us make a rapid survey of the balance sheet. When the Act came into force in 1956, many people thought that, in so far as the managing agency system was concerned, it was the beginning of the end. The supply of industrial finance was no longer the monopoly of managing agents. The financial gap, if any, was being successfully bridged by a number of special institutions. Moreover, thanks to the climate created by the massive expenditure undertaken by Government to develop the country as quickly as possible, investors had shed their proverbial shyness and it was no longer difficult for a really sound concern to get the requisite funds through public subscription. It looked as if there was no *raison d'etre* for the survival of the managing agency system.

The present author, however, never shared this gloomy view. Writing immediately after the Act of 1956 came into force, he had remarked as follows: 'While it would be foolish to dogmatise on an issue of this kind, no such adverse consequence is likely to follow merely as a result of the restrictive provisions of the Act. It is true that, under the new scheme of things, managing agents would no longer be able to make the high profits they were making so long. But the maximum still permitted (viz. 10 per cent of net profits) is a sizeable remuneration and will continue to attract private enterprise. Secondly, the provisions of the Act relating to Secretaries and Treasurers afford an opportunity to existing managing agencies to transform themselves into these more acceptable functionaries. It is true that Secretaries and Treasurers would be entitled to only $7\frac{1}{2}$ per cent of net profits as remuneration;

Bill. Similar views were expressed—but in much stronger language—by Mr. T. K. Chaudhuri in a separate note of dissent.

[1] Vide the speech of Mr. Lal Bahadur Shastri, Commerce & Industries Minister of India, while introducing the Companies (Amendment) Bill, 1959, in the *Lok Sabha*.

they would have no right to appoint directors; and, lastly, they would have no right to sell goods manufactured by a company nor purchase machinery, stores or raw materials, nor trade in them. These, however, are *minor* curtailments of existing privileges and are not likely to have any adverse effect on the *essence* of the system.'[1] The author is happy to record that his forecast has turned out to be substantially correct.

The most vital section in the Act, affecting the continuance of the managing agency system, is Section 324, under which the Central Government could assume the power to make a notification declaring that with effect from a specified date or from 15 August 1960, whichever was later, no company engaged in any specified industry or business should have a managing agent. This provision was against the spirit of the Company Law Committee's recommendations. As is well known, it was added by the Joint Select Committee of the Parliament to placate the extremist demand for immediate abolition of the system. Since then, Government framed Rules which provided ample safeguards against any hasty action. These Rules laid down in detail the factors to be considered and the procedure to be followed before a notification could be issued. A Committee of Enquiry had first to consider the position and report to Government. The lines along which the Committee should proceed on its enquiry were also prescribed. These included consideration of the nature and present state of the industry, its importance in the national economy, its future prospects, the chances of its continued growth under other forms of management, and the financial standing, record and performance of the companies managed by managing agents. After the Committee of Enquiry had reported, Government was to refer the matter to its Advisory Commission which, in its turn, could hold a further enquiry and then advise Government on the necessity for, and advisability of, issuing a notification. Even so, the recommendations of the Commission of Enquiry and the Advisory Commission were not mandatory: Government might, if it so chose, reject or modify them.

[1] Vide the Second Revised Edition of the author's *Industrial Enterprise in India*, published in April, 1956.

So far, Government has not found it necessary to assume the powers under Section 324, because it has ample powers under Section 326 which requires that the appointment of a new managing agent or the re-appointment of an old agent must have its prior approval. During the period 1 April 1956 to 15 August 1960, Government gave its approval to about 1,345 such applicants. Although this figure is less than half the number of managing agencies that were in existence in 1954-55 (the exact number on this date, according to the Department of Company Law Administration, was 3,944), the very fact that Government did accord its approval in so many cases (and some more are said to be still pending) indicates that it was not unaware of the importance of this specialised organisation in the economy of the country.

It cannot be denied, however, that since 1956, managing agents have been subjected to various statutory regulations and restrictions. For example, in an extension of the principle that only 'fit and proper' persons should be allowed to function as managing agents, even in existing agreements which have been, or are being , renewed, the heir or devisee of the managing agent is permitted to hold office only if the Government is satisfied that he is a fit and proper person.[1] The requirement of Government approval to any transfer of office by managing agents and the provision that no resignation should be permitted until the managing agent has submitted certain documents to the Board of Directors and the latter has accepted them as satisfactory, have also provided a salutary check on trafficking in managing agency rights.

The most important check has been that on the remuneration of managing agents. It may be mentioned here that, even before the Act of 1956 was passed, Government had come to regard 10 per cent of the net profits as the ceiling for the remuneration of managing agents. Although this ceiling has been rigorously enforced by Government, it has not led to a wholesale winding up of this form of corporate enterprise. The managing agency system appears also to

[1] The Act prohibits the inclusion of any provision for succession to office by inheritance or devise in the case of *new* managing agency agreements pertaining to public companies and private companies which are subsidiaries of public companies.

have survived a further shock in 1959, when Government introduced a slab system of remuneration. Under this system, the remuneration of managing agents would be according to a sliding scale ranging from 10 per cent of net profits to 4 per cent, the percentage remuneration declining with increase in the absolute amount of net profits.

It would be interesting to note in this connection the results of some studies recently conducted by the Reserve Bank of India in regard to managing agency remuneration. The studies relate to the years 1955, 1956, 1957, 1958 and 1959 and cover some 700 public limited companies. Although the coverage for the four years is not in respect of identical groups of companies, and although the figures of managing agency remuneration do not include earnings from other sources such as sale or purchase of goods and supply of services, the progressive decline is significant.[1]

Managing Agency Remuneration Percentage of Profits before Tax

Year	No. of Companies covered	Percentage
1955	749	14.3
1956	736	11.2
1957	690	11.5
1958	665	9.9
1959	630	9.1

What then is the future of the managing agency system? The Act of 1956, by itself, imposed no obligation on Government to arrive at any decision regarding the future of the system. Section 324 merely provided the instrument through which such a decision could be implemented, if and when it was made. The fact remains, however, that although the Companies Act Amendment Committee suggested in 1957 that Government should formulate a definite policy by 15 August 1960, it has not done so. It is obvious that Government's attitude in this respect is pragmatic: unless something unforeseen happens, managing agents will continue to play their part within the framework of the Act.

As has been aptly pointed out by the National Council of Applied Economic Research, New Delhi, the advantages of the system, as well as its popularity, are derived from the

[1] Monthly Bulletins of the Reserve Bank of India, Bombay.

current shortages in the economy. With such changes as the growth of a managerial class and the development of specialised agencies for financing and promotion, the coverage of the system is bound to shrink.[1] On the other hand, it is evident that managing agents still make a significant contribution in two directions: (a) provision of risk capital to managed companies both from their own resources and by attracting savings through the capital issues market, and (b) expansion of existing enterprises under their management. The managing agency system has still an institutional role to play in the effective performance of the private sector.[2]

The story of the last five years points to a significant moral, viz. that entrepreneurs in India as represented in the managing agency firms have shown themselves capable of a resilience which has confounded their friends and critics alike: they have been able to rise to every new challenge which has been thrown at them.

Directors and Limitations on their Powers under the Act

The second important set of provisions in the new Act were those relating to Directors and their powers. The safeguards relating to managing agents had been provided because many of them took undue advantage of their position as managers of industry. While there were no malpractices on a similarly large scale by the Boards of Directors of joint-stock companies in India, cases had occurred where some directors tried to monopolise the Board for themselves, and also managed their concerns inefficiently or dishonestly. Provision was accordingly made in the Act designed to give the shareholders some ultimate control over the Board of Directors.[3]

The new Act prescribed that public companies should have at least three directors and private companies which

[1] For example, of the 4,356 *new* companies registered during the period 1956-57 to 1959-60, only fifty went in for the managing agency form of management.

[2] Vide National Council of Applied Economic Research, *The Managing Agency System*, New Delhi, 1959. Although this study was undertaken at the instance of the Federation of Indian Chambers of Commerce and Industry, New Delhi, the Council made an objective and independent analysis of its own and many of its observations did not fall in line with the declared policies and objectives of the Federation.

[3] It would be interesting to recall that the Amendment Act of 1936 also contained several provisions (*a*) limiting the powers of Directors and (*b*) enlarging the powers of shareholders.

are subsidiaries of public companies, at least two. Only an individual, and not any firm or company, could become a director. In the case of public companies, and their subsidiaries, not less than two-thirds of the total number of directors were to be persons whose period of office was liable to determination by rotation: and, every year, one-third thereof was to retire by rotation. In connexion with the election of directors, there was to be a separate resolution for each director. An interesting provision of the Act was that for minority representation on the Board: the Statute included a permissible provision in the articles of a company whereby not less than two-thirds of the total number of directors might be elected according to the principle of proportional representation.[1]

Restrictions were also placed on eligibility to directorship. Officers and employees of the company or of its managing agents or their subsidiaries, and co-sharers in the managing agency remuneration, were not eligible for election as directors in the two-thirds quota reserved for shareholders except on the authority of a special resolution passed after 'special notice' as required by the Act. As under the old Act, undischarged insolvents, persons of unsound mind and convicts were not eligible for appointment as directors.

An innovation in the new Act was that no person who had attained the age of 65 years could be appointed as a director, unless the shareholders specifically approved of the same by a resolution passed after special notice. Another innovation was the ceiling on the maximum number of directorships that a person could hold: the ceiling was fixed at twenty directorships. Finally, the shareholders were given power to remove any director before the expiry of his office.

The Act imposed several other restrictions on the powers of directors and the manner in which they were to be exercised. The Board was expected to meet at least once in three months. Certain powers could be exercised only by the Board as a whole. The power to make calls, to issue debentures or borrow moneys otherwise, to sanction contracts in which any director is interested, to invest in shares and debentures

[1] In a great majority of the federating States of the U.S.A., the method of election according to the principle of proportional representation is in vogue.

of companies under the same management, to appoint as manager or managing director a person who was already occupying that position in another company, and to fill casual vacancies in the Board—all these powers could be exercised only by the Board at Board meetings, and not by any individual director. Appointments of sole selling agents made by the Board had to be approved by the shareholders in a general meeting within six months of the appointment. Finally, in the case of public companies and their subsidiaries, the directors could not, without the consent of the shareholders by ordinary resolution, (*a*) sell, lease or dispose of the whole or substantially the whole of the undertaking, (*b*) remit or extend the time for repayment of any debt due by any director, (*c*) invest otherwise than in trust securities the sale proceeds of the undertaking or its property or premises, (*d*) borrow moneys beyond the paid-up capital plus the free reserves of the company [1] and (*e*) contribute to charitable or other funds (not connected with the business of the company or the welfare of its employees) more than Rs 25,000 in any financial year, or in excess of 5 per cent of its net profits on the basis of an average of the three preceding years, whichever was greater.

Under the old Act, loans to directors and to firms and private companies with which they might be connected were prohibited. The new Act extended this restriction further: in addition to the above restrictions, loans to any body-corporate the directors of which were accustomed to act in accordance with the directions or instructions of any director of the lending company, might be made only with the consent of the Central Government.

The Act prescribed a ceiling of 11 per cent of the net profits as the *total outgo* from a company (public companies and their subsidiaries) on account of the remuneration of its directors, managing agents, secretaries and treasurers, managing directors and managers. [2] Managing directors and

[1] Temporary loans from bankers in the ordinary course of business were excluded for this purpose.

[2] In computing this ceiling, sitting fees given to directors for attending Board meetings are excluded. This ceiling was not intended to apply in the absence or inadequacy of profits, but the total outgo in that case must not exceed Rs 50,000 per annum. The Central Government was, however, empowered to relax this restriction in appropriate cases so as to permit a higher remuneration.

directors in the wholetime employment of a company might be remunerated at a percentage of the net profits, but such percentage was not to exceed 5 per cent where there was only one director and 10 per cent in the aggregate where there is more than one such director. Other directors whose remuneration did not include any monthly payment might be paid a commission on the net profits of the company, provided this was authorised by a special resolution of the shareholders, and the total outgo from the company on this account did not exceed one per cent of the net profits where the company was managed by a managing agent, managing director, manager, secretaries or treasurers or a wholetime director, and three per cent in other cases.

The scheme of company management as envisaged under the new Act was that the immediate responsibility for ensuring that the management was conducted in accordance with the provisions of the law should be on the directors. Accordingly, the Act imposed severe penalties on directors for certain defaults. A company directorship, therefore, entailed responsibilities of a much more onerous nature than ever before.

These limitations on the powers of directors were bitterly criticised. It was said that these special liabilities and responsibilities had been borrowed blindly from the English Act, but the traditions of company management in India were different. It was asserted that they were unnecessarily stringent and that they would deter good and reasonable men from serving on Boards of Directors in future.[1]

The provisions of the Act which came in for the largest measure of criticism particularly from the business community, were those relating to (*a*) the right of a minority of shareholders to representation on the Board of Directors, (*b*) the prescribing of a maximum age limit of 65 years for directors, and (*c*) the ceiling on the total remuneration which could be paid to directors, managing agents, secretaries and treasurers, managing directors and managers. It was asserted, for instance, that minority representation in the manner contemplated under the Act (under certain circumstances,

[1] Memorandum of the Federation of Indian Chambers of Commerce and Industry, New Delhi, on the Indian Companies Bill.

Government was empowered to nominate directors to represent the interests of 'minority' shareholders) went against all principles of democracy and smacked of the 'reservation of seats for minority interests' in the political sphere. As regards the prescribing of a maximum age limit of 65 years for directors, it was pertinently asked why no such age limit was fixed in regard to the appointment of Ministers and Deputy Ministers under Government.[1] Finally, it was asserted that the ceiling on the remuneration which could be paid even to managing directors, managers and wholetime directors, coupled with the severe penalties which may be imposed on directors for defaults under the Act, would deter many honest and peace-loving people from accepting directorship of joint-stock companies, and, as a result, management would become the poorer.[2]

Were these criticisms valid? In the opinion of the author, they were not. A careful perusal of the so-called restrictive provisions would show that they were enacted in the best interests of company management in the country. They merely sought to regulate the conduct of directors, and not one of the provisions could be said to be unusual. As the Board of Directors was the ultimate authority, it was desirable that its duties and responsibilities should be clearly defined, and its powers regulated, in the public interest. As was pointed out by the Finance Minister in his speech before the Lower House of Parliament on 10 August 1955, abuses in company management had occurred not merely in companies managed by managing agents but also in companies managed by directors : hence the need to impose certain restrictions on the latter as well.

As regards the vexed subject of remuneration, it was true that the scale of remuneration to be received by managing directors, managers and directors was considerably reduced, but this has not deterred honest entrepreneurs from coming forward to play their part in the private sector. Moreover,

[1] The prescribing of the retiring age of Directors has become a farce. Almost all companies have automatically passed the requisite resolutions for re-electing over-aged Directors, and one is struck by the special pleading made on behalf of aged men who ought to retire!

[2] Memorandum submitted by the Bengal Chamber of Commerce and Industry, Calcutta, on the Indian Companies Bill.

the business community in India cannot afford to consider itself a class apart from the rest of the society. When the avowed goal is the establishment of a society in which inequalities of wealth and income must be reduced to the minimum, no patriotic business man could stand aloof or refuse to play his part.

Other Duties and Obligations under the New Act

The third important set of provisions related to other duties and obligations, safeguarding the interests of shareholders, actual and potential. The provisions regarding managing agents and directors also meant, in effect, additional power for shareholders, but, besides these, some other specific safeguards had to be provided.

For instance, the new Act made many changes of a significant nature in regard to the prospectus. These closely followed the provisions of the English law on the subject. Under the new Act, the information to be given in the prospectus was more extensive than under the old Act; and, in addition to civil liability, criminal liability up to two years' imprisonment with or without Rs 5,000 fine was prescribed for certain mis-statements. Among the new items of information to be given in the prospectus, mention may be made of the following: (*a*) the prospectus must show the subscribed capital of the managing agent (where the prospectus is issued, on behalf of the managed company, by a firm of managing agents); (*b*) the time of opening of the subscription lists should be disclosed in the prospectus; (*c*) the substance of any contract or arrangement whereby any option or preferential rights of any kind are given, or proposed to be given, to any person to subscribe for any shares or debentures should also be disclosed; (*d*) in respect of any property to be acquired, the prospectus should disclose the nature of the title; (*e*) the prospectus should give information about the general nature of every material contract and not merely some specific contracts; (*f*) in regard to preliminary expenses, the prospectus should disclose the persons by whom such expenses have been, or will be, paid, as also details of the expenses of the issue and the persons by whom they would be paid; (*g*) in the case of a company which has already been carrying

on business, or where it is proposed to acquire a business which has been carried on for less than three years, the prospectus should disclose the length of time during which the business has been carried on; (*h*) if any reserves or profits of the company or any of its subsidiaries have been capitalised, particulars of the capitalisation should be given in the prospectus; and (*i*) the prospectus should also disclose particulars of the surplus arising from revaluation of the assets of the company or of any of its subsidiaries during the two preceding years, and the manner in which such surplus had been dealt with.

The Act also required reports of accountants and auditors to be attached to the prospectus, in regard to certain matters, on the lines of the English law. Another restriction imposed by the Act in regard to the prospectus was that, if a prospectus was issued which included a statement purporting to be made by an expert, the written consent of the expert to its issue should be obtained, and, further, the expert should be one not connected in any way with the formation, promotion or management of the company. Finally, if the 'minimum subscription' was not subscribed within 120 days of the issue of the prospectus, then the moneys were to be refunded to the applicants within ten days thereafter.

A major change introduced by the Act—and one that had no parallel in the laws of any other country in the world—was the restriction on the kind of shares that might be issued. The Act did away with 'deferred shares'[1] or any type of share carrying disproportionate rights in regard to voting, dividend or other privileges. There were to be only two kinds of shares in the future—equity and preference. All voting rights were to be proportionate to the amounts paid up on the shares. The Act also provided an appellate machinery to deal with those cases where a party felt aggrieved by the refusal of directors to register a transfer of shares.

The old Act contained very few provisions in regard to shareholders' meetings. The new Act regulated this matter in some detail. The Registrar was given power to extend the time for holding the meeting under certain circumstances. On

[1] Existing 'deferred shares' were brought in line with the new provisions within a year of the commencement of the new Act.

the other hand, the Central Government was empowered to direct the calling of an annual general meeting where there had been default in holding one. The length of notice required for calling shareholders' meetings was increased from 14 to 21 days; and it was provided that the notice should specify not only the date, place and hour of the meeting, but also all material facts in regard to any special business to be transacted at the meeting. To enable shareholders hailing from distant places to exercise their membership rights effectively, the Act permitted even non-members to be appointed as proxies. Further, members having several votes were henceforward to be permitted to cast some only of their votes if they so chose, and they were also to be at liberty to cast some votes in favour and some against.

Under the old Act, three kinds of resolutions were recognised in respect of a shareholders' meeting, i.e. Ordinary Resolutions, Extraordinary Resolutions, and Special Resolutions. The category of 'Extraordinary Resolutions' was abolished under the new Act, and in its place was introduced a new category called 'Resolutions requiring special notice'. In respect of this new category of resolutions, notice of the intention to move the resolution had to be given not less than 28 days before the meeting. The definition of 'Special Resolutions' also underwent a substantial change, the requirement now being that the number of votes cast in favour of the resolution should be three times the number cast against it.[1]

The Act introduced several new provisions in regard to accounts. The more important changes related to the responsibility for ensuring that proper accounts were kept, which was now fixed on directors and managing agents. Another major change was in regard to the accounting provisions relating to holding companies and subsidiary companies. The balance sheets of holding companies were to show not only the Balance Sheet, Profit and Loss Account and Auditors' Report of their subsidiaries, but also several other statements and particulars.

In regard to audit, the changes made in the Act closely

[1] It may be mentioned incidentally that the matters in regard to which the consent of shareholders by special resolution is required are many more under the new Act than under the old Act.

followed the provisions of the English law. An auditor, once appointed, would, by virtue of the new provisions, get a sort of semi-permanence; for it would be extremely difficult to dislodge him under the new procedure. Further, the Central Government could appoint an auditor if a company failed to do so. The auditor was now given statutory right to receive notices and other communications relating to general meetings, and speak thereat on matters with which he was concerned as auditor. Finally, the auditor was henceforward to certify that the Balance Sheet and Profit and Loss Account reflect a 'true and *fair* view' of the affairs of the company, and not a 'true and *correct* view', as hitherto.

One of the weakest points of the old Act was the laxity of provisions relating to inspection. The conditions to be fulfilled before Inspectors could be appointed were extremely difficult to comply with, and the result was that, even in cases of gross mismanagement, the shareholders were unable to do anything effective and the Registrar was a mere onlooker. This lacuna was removed in the new Act. Any two hundred members could now apply for the appointment of an Inspector. Further, under certain circumstances (this is wide enough to cover almost all contingencies), the Central Government could, on its own initiative, appoint Inspectors. The Inspectors were also given wide powers under the new law: they could, for instance, where they considered it necessary, inspect the affairs of allied concerns. The procedure for launching prosecutions or resorting to other effective methods to protect the interests of shareholders was also considerably simplified.

A Summing-up

These rather far-reaching provisions gave rise to considerable misgivings among the business community in India. It was argued that, in their anxiety to safeguard the interests of shareholders, the rights of the directors and managing agents had been sacrificed and the door had been laid open for harassment by individual hostile shareholders. A close analysis of the new provisions shows, however, that they do not afford much opportunity to a minority of hostile and reckless shareholders to stir up trouble against the manage-

ment. The provisions may have been slightly 'inconvenient' to the management, but they have not made administration 'difficult'. Of course, if a majority of shareholders were to take up a hostile attitude, then they could make things awkward for the management, but if such a state of affairs ever took place, it would perhaps be more logical to conclude that something was really wrong with the management. The experience of the last five years has completely disproved the fears of the business community in regard to the possible disruptive powers of a minority of shareholders. Not a single instance has come to light in which the legitimate wishes of a majority have been thwarted by such a minority.

On the other hand, what strikes an impartial observer is that much of the 'protection' given to shareholders exists on paper only. Being widely dispersed, shareholders can hardly exercise any effective control on the Board of Directors. As long as they get a reasonable dividend, they are content to leave decisions to be taken by the Board. The number of 'special resolutions' which are passed at the annual general meetings of the various companies without even a single voice of dissent from the shareholders, proves conclusively that even the best-intentioned Act cannot provide adequate safeguards to persons who are, by nature, indolent and apathetic. As has been pointed out in the Report of the Department of Company Law Administration for the year ended March 30, 1961, many companies still resort to ingenious ways of diverting company funds to purposes not strictly connected with the business of the company. In addition to the vigilance exercised by Government, there is, therefore, a great need in the country today for setting up an organisation to look after and protect the interests of shareholders.

Chapter VII

ADMINISTRATION OF THE COMPANIES ACT

Historical Background

As has been noticed already, the weakest feature of company law in this country prior to the enactment of the new legislation lay in the administration of the Act. The Company Law Committee had referred to this fact in pointed terms in their Report. 'We have received numerous complaints from the representatives of the business community as well as of shareholders and the general public about the inadequate and perfunctory manner in which the provisions of the existing Act relating to inspection and investigation were administered. Some of them went so far as to suggest that the Indian Companies Act was, perhaps, the most unadministered of the Central Acts relating to trade and industry.' Indeed, the memoranda submitted by the various Chambers of Commerce to the Company Law Committee pointed out that 'even the existing provisions had not been adequately utilised by Government in appropriate cases' and that 'the malpractices which have ensued flow not so much from the absence of powers under the existing Act as from the dilatoriness of their exercise.'[1] As a matter of fact, there was no proper Central Authority to administer the Act as it stood.

Recommendations of the Company Law Committee

The Company Law Committee, therefore, suggested that a Central Authority should be created by statute to administer company law. The case for a *Central* authority was based on the following considerations. Firstly, the working of joint-stock companies has a very close bearing on the economic development of the country, and it was not possible for State Governments to take that comprehensive view of the economic terrain which the Central Government alone could. Secondly, the necessity for a uniform policy called for uniform administration of the instruments of that policy. Thirdly, the historical reasons which underlay the decentralisation of the

[1] Quoted by the Company Law Committee in their Report.

administration of the Indian Companies Act, no longer existed. Lastly, the financial argument which, in the past, induced the Central Government to transfer their powers or duties to State Governments was neither valid in actual practice nor could this be used as an argument against the setting up of suitable administrative machinery.

The justification for setting up an *effective* organisation for continuously watching the activities of joint-stock companies was stated thus by the Committee itself under five principal heads. Firstly, 'the law can function only through the formulation of precise definitions—definitions not merely of concepts or categories, but also of conditions or circumstances in which certain provisions would be applicable, while in others they would have no relevance. Unfortunately, no definition, however well-drafted, can comprehend the multitude of characteristics that really matter, while the characteristics that matter may themselves vary from case to case. The intention of the law may thus be frustrated, both because it is often impossible to include all relevant examples or types, and also because astute lawyers can evade the law by superficial clauses, leaving the real character of a transaction unaffected.' Hence the need for continuous watch by a properly constituted and organised authority. Secondly, 'while law must necessarily frame definitions of concepts, categories and the relevant conditions or circumstances in more or less *general* terms', only an appropriate authority could apply the law to marginal cases or decide in which cases relaxations can be made. Thirdly, 'the history of company law in this country shows how amendment of the Indian Companies Act has always lagged many years behind current practices in company formation and management. Only an appropriate organisation, whose function is to maintain a close watch over the working of joint-stock companies, can oversee the operation of the Companies Act, keep track of new tendencies and developments and recommend suitable changes in the existing law.' Fourthly, 'even the most well-conceived and well-designed law is liable to become ineffective and to fall into disrepute, if there is no regular machinery for making any use of it.' Fifthly, 'the general lack of financial knowledge and of alertness on the part of investors and the general

public in this country, makes it all the more imperative that there should remain in existence an authoritative body to keep a continuous watch over company promotion and management.'[1]

Following, therefore, the example of the U.K., where the Board of Trade functions as the authority for the control and supervision of the working of joint-stock companies, and of the U.S.A., where the corresponding functions are discharged by the Securities and Exchange Commission, the Committee recommended that a Central Authority should be set up in India as well. The Committee then considered the advantages and disadvantages of the two alternative types of such authority, viz. a Central Department dealing with joint-stock companies on the same lines as the Board of Trade in the U.K. and a Central Statutory Authority on the model of the Securities and Exchange Commission of the U.S.A., and decided in favour of the latter. It suggesed that the statutory authority should be called 'The Corporate Investment and Administrative Commission',[2] and that it should consist of a Chairman and not more than four members who should combine suitable administrative experience, practical knowledge of company law and knowledge of company finance and accounts.

As regards the functions of the Commission, the Committee's views were that it should (*a*) carry out such duties as might be entrusted to it under the new Companies Act, (*b*) keep the investment markets in the private sector of the economy under continuous observation, (*c*) carry out such other functions relating to capital issue control, regulation of stock exchanges and any other subject connected with the promotion and formation of joint-stock companies as might be delegated to it by the Central Government and (*d*) build up a cadre of trained technical and administrative staff competent to analyse and study prospectuses, company accounts and problems of investment finance. For the field

[1] *Report of the Company Law Committee*, New Delhi, 1952.

[2] This name was suggested because, according to the Committee, the proposed Commission should not merely administer matters that arise out of the working of joint-stock companies under the Indian Companies Act, but also maintain a close and continuous watch over the investment market 'from the earliest stage of the promotion of a company to its management and final dissolution.'

organisation, the Committee recommended that the country should be divided into a suitable number of regions, with wholetime Registrars and adequate staff to support them.

Central Department aided by Advisory Commission

The Bill which was introduced in the Legislature did not provide for a Statutory Central Authority as recommended by the Company Law Committee. The Select Committee, however, considered the matter, and felt that it would be better to place the responsibilities for the due fulfilment of the functions under the Act squarely on the Central Government. It, therefore, stuck to the scheme, proposed in the Indian Companies (Amendment) Act of 1951 (Act LII of 1951) and re-introduced in the draft Bill, a provision under which an *Advisory* Commission was set up to *advise* Government in regard to the exercise of the various powers conferrd on it by the Act.

It was this departure from the recommendations of the Company Law Committee which evoked the severest criticism. It was argued that departmental control would be dilatory and obstructive. 'The approval of Government on the most meticulous detail would not only hamper the functioning of private enterprise but might allow some of the evils and abuses to invade the administration also, since the fates and fortunes of companies and individuals would be involved.' Prior consultation with the Advisory Commission would not be an adequate safeguard, nor would the provision that, in some matters, the orders passed or notifications issued or rules framed, would have to be laid before each House of Parliament.[1] Secondly, while major issues of economic policy should certainly be determined by Government, a Statutory Authority would, according to many, have created more confidence and possessed greater elasticity and initiative than a Central Department. 'Only a Statutory Authority can maintain its independent character and avoid suspicion of bias or partnership in the discharge of its functions.' Even

[1] Although the latter provision gives an opportunity to Parliament to raise any issue by motion—on the analogy of the 'prayer' motions in the House of Commons—the House can act only after the executive has exercised its authority, and such action may not be effective. Then there are groups of cases in which consultation with the Advisory Commission is not obligatory at all.

those who felt that the new Act did not go far enough in regard to its penal provisions felt extremely unhappy that the Select Committee had not recommended the establishment of a Statutory Central Authority.[1] 'The scheme proposed by the Select Committee vests large-scale powers in various matters in a Government department. This would create pressure-group politics in collusion with interested groups and departmental executives.'[2]

Central Department of Company Law Administration

Notwithstanding the above objections, the recommendations of the Select Committee were accepted almost *in toto* by Parliament, and the Bill as amended by the Committee became an Act. Government's 'case' for departing from the recommendation of the Company Law Committee was that, 'having regard to the basic economic importance of the Companies Act to the functioning of the private sector, Government could not possibly divest themselves of their responsibilities for the administration of the Act by delegating the same to a Statutory Commission, over which Government could have at best only a limited and perfunctory control.' The Select Committee took the view that, in practice, it was not possible to separate the economic and technical aspects of the administration of the Companies Act and, therefore, decided that both must remain the direct responsibility of Government.[3]

In accordance with the provisions of the Act, a new department known as the Department of Company Law Administration, was created within the Ministry of Finance, Government of India, with a full-fledged Secretary in charge and directly responsible to the Minister concerned. The responsibility of

[1] Vide 'Minutes of Dissent' of (*a*) Messrs. M. S. Gurupadaswamy, V. K. Dhage, B. C. Ghose and Amjad Ali and (*b*) Mr. T. K. Chaudhuri.

[2] The Finance Minister himself admitted, in his winding up speech after the third reading of the Bill, that the assemblage of powers vested in Government was 'enormous and probably without parallel elsewhere.'

[3] In support of Government's stand, Mr. C. D. Deshmukh quoted the following views of Mr. Cohen, Chairman, of the Cohen Committee in the U.K.: 'No modern system of company law can be satisfactorily administered except through a strong and competent civil service, for, it is the essence of any such system that effective powers must be given to the execution and a large measure of discretionary authority must of necessity be vested in the organisation responsible for the administration of the Companies Act.'

this department consisted of the administration of the Companies Act and some other related subjects, e.g. Capital Issue Control, Stock Exchanges, Industrial Finance Corporation, State Financial Corporations, Industrial Credit and Investment Corporation and the regulation of the accountancy profession. In September 1956, however, the responsibility of the new department was restricted to the administration of the Companies Act and the regulation of the accountancy profession only. Later, in the year 1958, the department was transferred from the Ministry of Finance to the Ministry of Commerce and Industry.

Under the Central Secretariat at New Delhi, there were set up four Regional offices in charge of Regional Directors at Bombay, Madras, Calcutta and Kanpur, each looking after a group of offices in the States. These were in addition to the offices of full-time Registrars of Joint-Stock Companies in all the States of the Indian Union. The Regional Directors function as local representatives of the department in the regions allocated them and advise and guide the Registrars on technical and administrative matters. They also function as a link between the Central Government and the State Governments in the region. Conferences of Regional Directors and Registrars of Joint-Stock Companies are held annually for exchanging information and discussing problems arising out of the Act.

As required under Section 410 of the Act, an Advisory Commission with a full-time Chairman and four part-time members was also constituted on 1 April 1956.[1] The Commission enquires into and advises the Central Government on all applications made to the latter by companies in regard to matters specified in Section 411 of the Companies Act of 1956.

As we have seen, the fear was expressed in many quarters that concentration of so many powers in a single department might lead to bureaucratic tyranny. The officers of the department have, however, been exercising their powers with sympathy, understanding and imagination. Their efforts have been directed towards removing (*a*) marginal obscurities in the language of the law through interpretational guidance,

[1] The Commission was reconstituted in March 1959.

and (*b*) avoidable difficulties in the day-to-day working of the Act by suitable procedural adjustments wherever possible. During the first three years (1956-57, 1957-58 and 1958-59), the department adopted a deliberately lenient attitude in regard to acts of omission and commission and it was only when Government felt that the provisions of the Act had become widely known and been properly understood that it issued orders for a more vigorous enforcement of the Act.

The tasks which the department had to discharge were not easy. Laxity in the administration of the Companies Act and related measures prior to 1956 had induced certain habits of thought and action in the corporate sector which could not be got rid of overnight. As a result, compliance even with those provisions of the Act which had been on the statute book for decades but had not been systematically enforced, was resented by some companies. The enforcement of the relatively new provisions of the Act evoked still greater resistance from certain quarters. The Annual Report for 1958-59 noted with regret that the social objective behind the new provisions was not seen even by the more enlightened management and that the sense of fiduciary responsibility was growing only tardily.[1]

An Assessment

Now that the Act has been in force for over five years, it may be asked whether it has helped or hindered corporate enterprise. When the new Companies Bill was under discussion in Parliament, Mr. C. D. Deshmukh, the then Finance Minister, claimed that 'the overall objective was one of growing hedges rather than finding fetters for private enterprise.' He even added that the powers Government was taking would prove to be a help and not a hindrance to legitimate business.

The business community and even some economists, however, thought otherwise. While they conceded that much would depend on the spirit in which the law was going to be administered, they asserted that the best law could become an instrument of bureaucratic dilatoriness, tyranny and even corruption. The fear was also expressed that the administration

[1] *Annual Report of the Department of Company Law Administration*, New Delhi, for the year ended 31 March 1959.

of the company law might be 'imbued with a high political equation'. Would the executive, which had been vested with such a vast array of discretionary powers, it was asked, be able to administer this admittedly difficult and complicated measure with the requisite degree of objectivity, impartiality and sympathy?[1]

We have stated earlier that the officers of the Department of Company Law Administration have so far exercised their powers with sympathy, understanding and imagination. Nevertheless, the business community in India does not appear to be reconciled to the measure. If the Public Opinion Surveys conducted by the Indian Institute of Public Opinion, New Delhi, are any guide, private entrepreneurs still seem to think that this 'mammoth and complex piece of legislation and a compromise of conflicting ideologies' has been a hindrance rather than a help. 'The Act is a vast jigsaw puzzle, beyond the comprehension of many business men. It contains so many penalties that those who wish not to get entangled must either keep out of joint-stock company business or spend enormous sums of money to get advice from expert lawyers and accountants. Even the smallest company must now have, on its staff, a specialist on company law—a luxury which so few can afford.'[2]

The figures of registrations of joint-stock companies since 1956, however, tell a different tale. Although for a few years new company registrations were considerably below the number of new companies floated in the period just preceding the coming into force of the Act of 1956, there has been a progressive increase since. As against 1,448 new companies registered in 1955-56, the number registered in 1957-58, 1958-59, 1959-60 and 1960-61 were 961, 1,095, 1,452 and 1,683 respectively. What is more significant is that the total authorised capital of 6,039 new companies registered during the five years ended 31 March 1961, was Rs 1,044.8 crores as against the authorised capital of Rs 786.7 crores of 7,043 companies registered during the five years preceding 1956-57.

[1] Vide *Quarterly Economic Report*, August 1955, issued by the Indian Institute of Public Opinion, New Delhi.

[2] As was wryly observed by *Commerce*, Bombay, in their Editorial dated 17 September 1955, 'the only section that can probably feel happy must be those belonging to the legal profession!'

The available evidence thus shows that, notwithstanding the earlier gloomy prophecies in certain business circles, the tempo of new company formation has not only been maintained but may well be accelerated. It is, however, significant that the preferences of the newly formed companies are overwhelmingly (98%) in favour of management by Boards of Directors or Managing Directors.[1]

It has been argued that progress would have been even more rapid if some of the restrictive provisions were removed. The present writer does not agree. It is not denied that, with a freer hand given to promoters, the number of new registrations would have increased, but it is doubtful if some of the new ventures would have been economically sound. It should not be forgotten that the history of corporate enterprise in this country is replete with instances of mushroom and fraudulent companies, and these flourished at a time when no 'restrictive' legislation was in operation.

Further Amendments of the Companies Act

This does not mean that the Act of 1956 is perfect and cannot be improved upon. Even before the Act was brought into force, its framers recognized that it might contain defects and deficiencies which would become apparent only with the efflux of time. 'It is in the essence of company law that it must not only grow with the growing needs of trade and industry, but also be reshaped from time to time to meet unforeseeable changes in company practice as may result either from developments in techniques of production or investment, or may be contrived by the wit of man to evade the provisions of the existing law. Indeed, the success of company law in any country depends on the promptitude with which it can adjust itself to meet changes in the structure and functioning of companies.'

Certain deficiencies in the Act of 1956 came to light as soon as the Department of Company Law Administration started administering it. It was also found that some companies were taking advantage of loopholes in the Act and had even engaged experts to advise them as to how to evade its obligations without actually transgressing the law. Accordingly,

[1] Vide Appendix V.

in May 1957, the Government appointed a Committee under the chairmanship of Mr. A. V. Visvanatha Sastri, a former Judge of the Madras High Court, to examine the structure as well as the contents of the Act, with a view not only to removing its defects and deficiencies but also ensuring better fulfilment of the purposes of the Act. The Committee submitted its report in November 1957 which the Government published and placed before both the Houses of Parliament in December 1957. The Committee did not suggest any major or radical changes: it merely tried 'to plug loopholes, supply omissions, clarify ambiguities, correct mistakes, remove inconsistencies, omit unnecessary or irrelevant provisions and add others conducive to the smooth and effective working of the Act.'[1]

The comments of the various Chambers of Commerce, employers', workers' and shareholders' organisations, and economists and experts were invited on the Sastri report and the recommendations contained therein. In the light of these comments and also of the experience of the working of the Act since the report had been submitted, a Companies (Amendment) Bill (Bill No. 37 of 1959) was drafted and introduced in the Lok Sabha on 1 May 1959. Some of the amendments were of a clarificatory nature, designed to remove drafting defects and obscurities which had caused difficulty in the interpretation of the statute; others sought to overcome practical difficulties experienced in the working of the Act; but a few were considered necessary 'to ensure the better fulfilment of the purposes of the Act and to remove lacunae in the existing provisions'. The Bill was referred to a Joint Select Committee of both the Houses. After having held twenty-seven sittings and discussed all the 210 clauses in great detail, the Committee reported back on 16 August 1960. The Bill was passed by Parliament in its winter session in 1960 and received the assent of the President on 28 December 1960.

The more important provisions of this amending Act are those relating to the (*a*) appointment of special Auditors by Government to make special audit of a company's accounts in certain specified circumstances, (*b*) imposition of some

[1] *Report of the Companies Act Amendment Committee*, New Delhi, 1957.

restrictions on the issue of shares and debentures and prohibition of the transfer of shares and/or debentures in certain cases, (*c*) grant of further powers to Government and its officials in regard to sole selling agencies, (*d*) further restrictions on the purchase by a company of the shares etc. of other companies, (*e*) closer regulation of inter-corporate investment and of investment companies, (*f*) prohibition of simultaneous appointment of different categories of managerial personnel, and (*g*) disclosure of information in regard to donations made by companies to the funds of political parties.

All these provisions were bitterly criticised by the representatives of the business community, at the Select Committee stage.[1] The objections were reiterated at the time of the clause-by-clause discussion of the Bill. 'These additional encroachments on the rights of the management and these measures of over-regulation by a bureaucracy, would further inhibit business enterprise. The sweeping power which Government is going to assume to conduct the special audit of a company is completely unwarranted and uncalled for. Entrepreneurs should be given a fair chance to live and to expand, to run their business using their own judgement, subject only to the control which is exercised by the investors, viz. the shareholders and subject only to minimum interference by Government.'

The reply of the Government was that shareholders were often not in a position to control the management, that existing powers under the Act had proved inadequate and that healthy development of joint-stock enterprise itself required that the loopholes which had come to light should be plugged to prevent further mischief. At the same time, it cannot be denied that Government is relying too much on legislation to put a stop to maladministration of joint-stock companies. If some companies are maladministered even today, this is due, at least in part, to the fact that the enforcement machinery continues to be ineffective and inefficient.

[1] Minutes of dissent were appended, among others, by Messrs. M. R. Masani, Naushir Bharucha, D. V. Patel, B. M. Chinai, P. D. Himatsingka and G. D. Somani—well-known protagonists of "free" enterprise or business men. The last three did not, however, object to the proposal regarding disclosure of information in regard to donations made by companies to the funds of political parties.

The present writer does not think that these further amendments would 'dampen the enthusiasm of entrepreneurs or make difficult the successful floatation of new companies'. As happened five years earlier, there may be a temporary setback, but private enterprise will soon adjust itself to the new restrictions. He also disagrees with the suggestion made by Mr. Asoka Mehta that a statutory body should have been set up to administer company law, along with an administrative tribunal to enforce it. 'The running of the companies is so closely related with the broad economic policy of the Government that it would not be advisable for the latter to vest these powers in some separate or independent body. There is no way out but to leave this matter to be handled by the appropriate department of the Government, viz. the Department of Company Law Administration.'[1]

Donations to the Funds of Political Parties

What is objectionable, however, is the provision requiring companies to disclose information in regard to donations made by them to the funds of political parties. Apart from the fact that it is morally undesirable that companies formed for the conduct of business should donate to such funds, the obligation to disclose this information gives an unfair advantage to the ruling party. In a controlled economy, the Government of the day has enormous powers over the fortunes of business and industrial enterprise. The possibility of selfish and unscrupulous elements in business seeking advantages for themselves by contributing to the funds of the ruling party is not hypothetical. And no business house would, under such circumstances, dare to contribute to the funds of a party which is in opposition to the Government. Hence, although on paper the amendment appears wise and harmless, it is certainly a blow to democracy.

The best course would have been to prohibit altogether all donations to political funds. This would have been desirable even from the standpoint of safeguarding the interests of the minority shareholders. Why, for example, should even one

[1] Speech of Mr. Lal Bahadur Shastri, Minister for Commerce & Industry, in the *Lok Sabha* on 18 November 1960, in connection with the Companies (Amendment) Bill, 1959.

shareholder be compelled to contribute an amount to the funds of a political party against his will, simply because the majority decides to make such a contribution? It would be worth while repeating here what was stated by the distinguished judge of a High Court in a recent case arising out of the donation made by a company to the funds of the Congress Party. 'To induce the Government of the day by contributing money to the funds of political parties is to adopt a sinister principle fraught with grave dangers to commercial as well as public standards of administration. Persuasion by contribution of money lowers the standrd of administration even in a Welfare State or a democracy. To convert convictions and conscience by money is to pervert both democracy and administration. Joint-stock companies are not intended to be adjuncts to political parties and possible sources of revenue for these parties. It will induce the most unwholesome competition between business companies by introducing a race on who could pay more to the political funds of a particular party. In that competition, business is bound to suffer in the long run. In the bid for political favouritism by the bid of money, the company which will be the highest bidder may secure the most unfair advantage over its rival trader companies. It will mark the advent and entry of the voice of big business in politics and in the political life of the country. This would be bad for both business and politics. It will be bad alike for public life as well as commercial life.'[1]

Unfortunately, politics has already invaded business in this country. As a result, although the proposal to prohibit donations to the funds of political parties was seriously urged in Parliament by the members of the parties of the right as well as of the left, the whip issued by the ruling party (Congress) carried the day. It is true that the quantum of political donations that could be made by a company in a particular year has been limited to Rs 25,000 or five per cent of the average net profits during the three preceding financial years, whichever is greater, but amendments seeking to nullify the provision or to publish the facts within one month, were rejected by

[1] Taking the law as it stood, the judge had to pronounce such donations as 'legal', but he made no secret of his view that he considered them highly immoral.

an overwhelming majority.[1] The only concession which Government made was that no such donations would be made from the funds of State undertakings.

On balance, it was an unfortunate stand that Government took. That similar practices are widely prevalent in many western democracies is no convincing argument that the practice is good. As was aptly stated, 'the plain truth is that a commercial company is not a charitable organisation and if a company makes a contribution to a political party's coffer, it does so either because the party asked for such a contribution to be made or because that company wants to create for itself a vested interest in that party.'[2] These are harsh words, but there are occasions when harsh words ought to be spoken.

[1] The first amendment was rejected by 122 votes to 45, the second by 132 votes to 47. Three members of the Congress Party, however, voted with the Opposition.

[2] Ramaswami J., in AIR 1960 Madras 257, remarked as follows: 'If we had in our country in consequence (of donations made to the funds of political parties) Governments which owed their positions directly and indubitably to the financial support received from these companies, we would have a Government of the people by industrialists for industrialists. That would not be democracy—not at any rate as Lincoln defined it.'

CHAPTER VIII

THE STORY OF JOINT-STOCK COMPANIES IN INDIA[1]

Growth of Companies up to the Twentieth Century

AS IN EVERY OTHER country, the development of modern industrial enterprise has been closely associated in this country with the progress of the joint-stock form of organisation. It would be interesting, therefore, to make a rapid survey of the progress made by companies established under the Companies Act and to examine whether they throw any light on the likely pattern of future development.

We have already seen that it was only in 1850 that the legal institution of joint-stock companies was first created in this country through an Act. The Act of 1857 recognised the limited liabilities of the 'corporate personality', while the Act of 1866 consolidated this principle in more precise and unambiguous language. Unfortunately, however, no agency was set up for a long time to collect even essential data in regard to joint-stock companies, with the result that statistical evidence for the first three decades since 1850 is completely lacking and only some fragmentary information is available for the next two decades in a solitary source named 'Statement exhibiting the Moral and Material Progress of India'. It was only in the early years of the present century that an annual publication relating to joint-stock companies was started, giving information in regard to the number and paid-up capital of companies at work for 28 industrial groups, but only for the major provinces of British India and one Indian State (Mysore). It was not until 1914-15 that information became available on new registrations and liquidations of companies registered in India as also in regard to companies registered elsewhere than in India, but working in India. A few years later, i.e. in 1920-21, the industrial classification was made more exhaustive, giving details for 59

[1] For the materials contained in this chapter, the author has drawn freely on reports issued by the Department of Company Law Administration, Government of India.

industrial groups instead of 28. About the same time, figures relating to many Indian States also came to be incorporated in the annual publication. The annual publication was further strengthened, some time in 1935-36, by a monthly publication on joint-stock companies which gave data regarding the new registrations, liquidations, and changes in the capital structure of existing companies, during each month.

At the beginning of the present century, there were 1,340 companies at work with a total paid-up capital of Rs 34.7 crores, as compared with 505 companies with a total paid-up capital of Rs 15.7 crores in 1882 and 950 companies with a total paid-up capital of Rs 26.6 crores in 1892. Between 1882 and 1900, therefore, the number of companies as well as their paid-up capital had more than doubled: the growth was particularly significant in the sphere of 'mills and presses' and 'trading companies'. The companies were concentrated primarily in Bengal, Bombay and Madras: their shares of paid-up capital, during 1899-1900, came to 92.9 per cent of the total for the whole country.[1] On an average, during the nineties of the last century, 150 companies were set on foot every year whereas there were 61 liquidations in a year.

Progress until 1956

The number of joint-stock companies increased steadily from the beginning of the present century, particularly after the Swadeshi Movement of 1905. In 1905, the number of companies was 1,550 with a paid-up capital of Rs 40.3 crores. This had increased, on the eve of World War I, to 2,744 with a paid-up capital of Rs 76.6 crores. During the first 15 years of the present century, therefore, the number of companies as well as their capital had more than doubled. Then came World War I and the post-war period of increased industrial activity. At the end of 1922, the number of companies had risen to 5,189 with a total paid-up capital of Rs 230.5 crores.

The next ten years, however, did not witness any spectacular rise in the number and paid-up capital of joint-stock companies. As against a three-fold increase in the paid-up

[1] The distribution was as follows: Bengal, 43.2 per cent, Bombay, 42.3 per cent, Madras, 7.4 per cent, the rest of India, 7.1 per cent.

capital during 1913-22 (i.e. from Rs 72.1 crores to Rs 230.5 crores), the rise during the following decade ending March 1932, was only to the extent of Rs 55.4 crores (i.e. from Rs 230.5 crores to 285.9 crores). The last four years of this decade were characterised by a severe trade depression which reflected itself in the liquidation of a number of joint-stock companies.

Between 1932 and 1939, an outstanding event was the separation of Burma in 1937, which reduced the number of companies working in India and their paid-up capital by 278 and Rs 25.7 crores respectively. Even so, the number of companies in 1939, i.e. at the beginning of World War II was 11,114 with a total paid-up capital of Rs 290.4 crores.

During the period of World War II, i.e. between 1939 and 1945, the number of companies rose to 14,859 with a total paid-up capital of Rs 389 crores, i.e. nearly Rs 100 crores more than at the beginning of World War II. The termination of the War gave a new fillip to company promotion in the country and there was an unprecedented growth in the number of companies, accompanied by a sizeable increase in their capital resources. On the eve of the partition of the country, the number of companies stood at 21,853 with a paid-up capital of Rs 487.7 crores.

Despite the fact that as a result of partition, 2,000 companies with a total paid-up capital of Rs 18 crores were 'lost' to India, the number of companies as well as the paid-up capital thereof registered an increase in the following year. Since then, the upward movement has been steadily maintained and at the end of March 1956, the number of companies stood at 29,874 with a total paid-up capital of Rs 1,024.2 crores.

The Position since 1956

Since 1956, the total number of joint-stock companies at work has fallen to some extent. This does not, however, indicate any diminution of activities in the corporate sector. The fall is the direct result of the administrative drive launched by the Department of Company Law Administration to weed out the moribund or inactive companies from the official records, which gave an incorrect and inflated

impression about the size of this sector. The total number of such companies was estimated at 6,500—7,500 at the time the Act of 1956 came into force. By 1959-60, about 4,500 of them had been removed from the registers.

The real state of affairs would be apparent from the figures of total paid-up capital which had gone up, between 1955-56 and 1960-61, by over 68 per cent, despite the weeding out of so many moribund companies.[1] This is as it should be, because the whole country is humming with industrial activity and it would have been very odd indeed if the statistics had told a different story.

The importance of the corporate sector in the national economy is brought out by the following further figures:[2]

A. *Share of Companies in the net Domestic Output* (1957)

Total net domestic output	.. Rs	11,360 crores
Output of joint-stock companies	.. Rs	1,300 crores
Share of companies ..	..	11 per cent

B. *Share of Companies in the Tax Revenue of the Central Government* (1959-60)

Gross tax demands ..	.. Rs	213 crores
Tax demands for companies	.. Rs	110 crores
Share of companies ..	..	51 per cent

C. *Share of Corporate Taxes in the Total Revenue of the Central Government* (1960-61)

Total revenue ..	.. Rs	938 crores
Corporate taxes ..	.. Rs	160 crores
Share of corporate taxes ..	..	16.3 per cent

D. *Share of Companies in the Factory Output* (1956)

Total output of all factories	.. Rs.	1,004 crores
Output of company-owned factories ..	.. Rs	922 crores
Share of companies ..	..	92 per cent

[1] Vide Appendix I.

[2] It may be stressed here that, compared to industrially advanced countries, India has still a long leeway to make up. In India, the share of companies in the total net domestic output works out at 11 per cent while the corresponding ratio in the advanced countries is over 50 per cent. It should not be forgotten, however, that the Indian economy still rests, and will continue to rest for a long time to come, primarily on agriculture and small and cottage industries outside the corporate sector.

E. Share of Companies in the Productive Capital of Factories (1957)

Total productive capital ..	Rs	544 crores
Productive capital of company-owned factories	Rs	507 crores
Share of companies		93 per cent

We thus see that, in terms of the use and deployment of the physical tools and resources of industrialisation, the corporate sector in this country occupies a clearly commanding position, notwithstanding its relatively small contribution to the aggregate national income.

The stature of the corporate sector has grown considerably during the last ten years and it still continues to grow. This would be apparent from the following two tables:

I. Share of the Corporate Sector in the Total Net Domestic Product at Factor Cost

	1948-49	1950-51	1956-57	1957-58
Share of the Corporate Sector in the total Net Domestic Product at Factor Cost	7%	8%	11%	12%
Share of the Corporate Sector in the total Net Domestic Product at Factor Cost for non-Government sector	8%	10%	12%	13%

II. Share of the Corporate Sector in the Total National Savings

	1950-51 (Rs crores)	1956-57 to 1958-59 (annual average) (Rs crores)	Rate of growth of annual average between 1950-51 and 1958-59 (percentage)
Absolute amount of savings in all Sectors	607	883	3.7
Savings in the Corporate Sector	35	33	3.4

The pattern of joint-stock companies at work also shows a healthy change. For a long time, a very large number of such companies were those engaged in trade and finance. As a matter of fact, even on the eve of independence, the latter type of companies constituted over 50 per cent of all companies at work. By 1957-58, the proportion had gone down to 39 per cent, while the proportion of companies engaged in processing and manufacture of various kinds and

in mining and quarrying had increased from 25 to 39 per cent. In terms of paid-up capital, the proportion had gone up even further—from 32 to 67 per cent, while that of companies engaged in trade and finance had fallen from 38 to 20 per cent. As regards the types of processing and manufacture in which these companies are engaged, there is an astonishing variety today, reflecting a further diversification of industrial development.

Statewise Distribution of Joint-Stock Companies

At the beginning of the present century, the three provinces of Bengal, Bombay and Madras accounted for 86 per cent of the total paid-up capital of all the companies in the country. Although these three States (i.e. West Bengal, Bombay and Madras) still continue to have the major share, it fell to 75 per cent in 1959-60. In terms of paid-up capital, the companies in these three States constituted 66 per cent of the total paid-up capital of all companies. The Statewise distribution of *new* companies registered during 1956-60 also shows that West Bengal, Bombay and Madras account for only 67 per cent of the total number of new registrations, while in terms of authorised capital, their share comes to only 54 per cent.[1] It is thus clear that the policy of Government in regard to the dispersal of industries in the less developed States of India is beginning to bear fruit.

A Note on the Dispersal of Industries

What were the historical factors which led to the concentration of industries in the above three States? The factors were that these were the centres where entrepreneurial talent (as embodied in the managing system) and capital were available. The cities of Calcutta, Bombay and Madras were also important railway junctions and ports, with the result that they had considerable advantage over other centres in the matter of assembly of raw materials and distribution costs.

In the course of years, these 'agglomerating' factors were partly neutralised by other factors operating in favour of other areas. New raw materials began to be exploited (e.g.

[1] Vide Appendices XV and XVI.

sugarcane in Bihar, bamboo and sabai grass in U. P. and Punjab, limestone in Kathiawar, Bihar and Punjab and iron ore in Orissa and Madhya Pradesh), and with the further expansion of transport facilities, Calcutta, Bombay and Madras no longer enjoyed the former monopolistic advantage. Freight rates of certain basic raw materials having been equalised, the cost factor in production no longer operated to the disadvantage of less favourably placed areas. Tremendous changes had also been brought about by the development of new forms of power, e.g. petroleum and hydro-electric energy, with the result that a coal area was no longer necessarily the most economic site for the setting up of a big heavy machinery plant.[1] On the other hand, the very fact that consumer demand in the country as a whole has increased has led to the setting up of industries in areas hitherto neglected by orthodox financiers and entrepreneurs.

To these may be added an active State policy to secure balanced development of the various parts of the country. The Industrial Policy Resolution of 30 April 1956, emphasised that disparities in levels of development between different regions should be progressively reduced. 'Concentration of industries in certain areas in the past was due to (*a*) availability of necessary raw materials or other material resources and (*b*) ready availability of power, water supply and transport facilities. But areas which are at present lagging behind need not remain so for ever.' The objective of 'reduction of inequalities of income and wealth and a more even distribution of economic power' has also reinforced the demand for dispersal of industries. Accordingly, while licensing new industries, Government now carefully considers whether, in the long-term interests of the country, it would not be wiser to have a balanced programme of dispersal, geared to the *anticipated*, and not merely *current*, needs of the various regions.[2] The licensing authority consciously tries to locate new indus-

[1] The harnessing of atomic energy, with the possibility of nuclear power being produced on a competitive basis, may make further changes in the pattern of industrial location.

[2] Vide the author's article entitled *Modern Trends in Industrial Location* published in the Proceedings of the Residential Study Course on Management for Higher Productivity conducted by the Indian Institute of Technology, Kharagpur, in February, 1958.

tries in areas away from the existing industrial centres. To give two typical examples, the sugar industry is now being spread out far away from the traditionally sugar-producing States, and the same policy is being pursued in respect of the textile industry.

CHAPTER IX

CONCENTRATION OF ECONOMIC POWER

Nature of Concentration of Economic Power in Other Countries

IN RECENT YEARS, a good deal of discussion has taken place on the alleged concentration of economic power in a few hands in the corporate sector. One of the four principal objectives of the Second Five-Year Plan was 'reduction of inequalities in income and wealth, and a more even distribution of economic power'. Analysing the concept, the Plan said that 'in the past, economic development often led to inequalities of income and wealth, firstly, because the gains of development accrued to a small class of business men and entrepreneurs and, secondly, because the immediate impact of the application of new techniques to agriculture and traditional industry generally resulted in unemployment and under-employment among large numbers of people'. It was, therefore, suggested that a more even distribution of economic power should be achieved through (*a*) the development of cottage and small-scale industries ('they offer a method of ensuring a more equitable distribution of the national income'), (*b*) the formation of co-operatives at various levels, and (*c*) State action in appropriate fields of economic activity.

Concentration of economic power is usually associated with monopoly. This has been particularly the case in the U. S. A. and, to some extent, in the U. K., Germany and Italy. In these countries, this concentration has manifested itself in the trust, the cartel and the holding company, and has even extended beyond national boundaries. In the U.S.A. in particular, concentration of economic power can be seen in the fact that a few large corporations (sometimes a few individuals) control most of the productive capacity and distributive machinery in that country. There were so many instances of restrictive practices, cartelisation, trustification and interlocking, both financial and managerial, that the U.S. Congress had to enact a series of legislative measures (e.g. the Sherman Act, the Clayton Act and the Federal

Trade Commission Act) to curb these unwholesome practices. Concentration could not, however, be halted. In 1958, 250 big corporations owned 45 per cent of the total assets owned by all the corporations in that country, and more than one third of the directorships in the latter were held by just 400 men. In the sphere of employment, less than one per cent of the corporations employed more than 50 per cent of the workers.[1]

The growth of these gigantic industrial units and combines was facilitated by certain facts and circumstances inherent in the economic situation—particularly by technological advance and increasing use of mechanical power. As markets expanded and consumer demand became more discriminating, the need was felt for more intensive research and also for a certain degree of understanding between firms producing identical or similar goods. In a sense, it was competition which paved the way for the elimination of competition.

Even so, it was not monopoly which emerged, but duopoly or oligopoly. In their endeavour to cater for an increasingly fastidious market, the bigger firms entered into common arrangements in regard to research, marketing and even the pricing of products. This 'fewness of sellers' did not necessarily mean exploitation of the consumer: as a matter of fact, the consumer benefited from the optimum allocation of economic resources and more efficient operations under the duopolistic or oligopolistic system. Nevertheless, it is also true that the very power of concentration tempted firms to resort to various kinds of restrictive practices, some of which at least were not in the public interest. These led to an enquiry into some aspects of this concentration by a National Economic Committee in the U.S.A. (in 1938-41) and the setting up of the Monopolies and Restrictive Commission in the U.K. (in 1948), followed eight years later by the passing of the Restrictive Trade Practices Act.

The question may now be asked whether concentration of economic power in the accepted sense is a feature of the Indian economy today. The fact that a major part of the

[1] A. D. H. Kaplan, *Big Business in a Competitive System*, Washington, 1959.

net product of industry is produced by a handful of large-sized companies has been cited as evidence of concentration of economic power.[1] The floatation of quite a few giant companies in recent years has also been held up as another evidence of a trend towards concentration. As stated later, neither of these provides a true criteria for judging or measuring concentration.

Floatation of Giant Companies in India

The trend in recent years has undoubtedly been towards the floatation of companies with bigger authorised and paid-up capital. The days of launching under-capitalised concerns are gone, as entrepreneurs have realised that, in the highly competitive world market, economies of production can be secured only in large units. From the frequency distribution of newly registered companies, during the period 1957-61, it appears that no less than 170 companies were floated with an authorised capital of Rs 1 crore and above.[2]

These giant companies comprised 111 public and 50 private companies having an authorised capital of Rs 301 crores and Rs 298.5 crores respectively. The authorised capital of these 170 giant companies accounted for about 72 per cent of the total authorised capital of all new registrations during the period under review. It is true that as many as 29 of these 170 companies are Government companies with a total authorised capital of Rs 283.5 crores, but even if these are excluded, the picture remains one of floatation of companies with much bigger authorised capital than, say, twenty or twenty-five years ago.

The same conclusion is reached if we consider the *average* paid-up capital of joint-stock companies since 1947. The average paid-up capital has registered a steady increase from Rs 2.19 lakhs in 1947 to Rs 6.60 lakhs in 1961.[3]

Even so, in comparison with the world's top industrial giants, the corporate "giants" in our country are very small

[1] In 1957, 5 per cent of such establishments produced over 60 per cent of the manufactures (in terms of value). Vide the author's article entitled '*The Ecology of Economic Power*' published in the *Indian Journal of Economics*, Allahabad (July, 1958).

[2] Vide Appendix XVIII.

[3] Vide Appendix I.

indeed. Whichever way they are measured, whether in terms of total assets, paid-up capital, total sales or net profits, the biggest companies in the private sector like the Tata Iron & Steel Co., Ltd. or the Associated Cement Companies, Ltd. are but dwarfs in comparison with such industrial combines as General Motors or Standard Oil of U.S.A., Royal Dutch/Shell or Unilever of U.K./Holland, or even Volkswagenwerk A. G. or Fried Krupp of West Germany.[1]

Secondly, with the launching of a number of heavy industrial projects by Government, these latter are gradually displacing companies in the private sector from their top positions. As will be seen from the first Table in Appendix XVII, in terms of total tangible assets (net of depreciation), the Hindustan Steel, Ltd., a Government Company, now heads the list of giant companies in our country, while three other companies in the public sector (National Coal Development Corporation, Sindri Fertilisers & Chemicals, and Hindustan Aircraft) also happen to be among the first ten. It is true that, in terms of total sales, these Government companies do not figure in the list at all, but the picture will change as production is geared up to installed capacity. One need not be surprised if, at the end of the Third Five Year Plan period, the first few places in both the Tables are coccupied by Government companies.

Foreign Companies in India

Contrary to popular belief, the number of foreign companies (i.e. companies incorporated elsewhere than in India) operating in India is still pretty large. At the end of March 1961, 580 such companies were functioning in India (as against 827 in 1947-48). About 75% of these have their origin in the Commonwealth countries (mostly the United Kingdom).

According to estimates made by the Reserve Bank of India, British investment stood in 1961 at £360 million as against £155 million in 1948. During the last five years (1957 to 1961), over 200 new British firms have joined hands with Indian companies, providing the technical 'know-how' to

[1] Vide Appendix XX.

them and, in quite a few cases, bringing in private capital also. An analysis of the activities of these firms shows that their production operations extend from various types of consumer goods to heavy engineering equipment, chemicals, cable wires and other accessories.

U.S. investment also is growing fast—as a matter of fact, at a faster rate than British investment. Still, it is only a fraction of the British capital invested in this country. The latest estimates show that American investment now stands at $180 million.

Some of these foreign companies are subsidiaries of giant companies with world-wide coverage. The question, therefore, arises whether they provide a favourable climate for the concentration of economic power in a few hands. The answer appears to be in the negative, as the Government is particularly vigilant about the operations of foreign companies in this country. At the same time, it cannot be denied that they wield a power much in excess of their operating capital.

Concentration of Control prior to the Act of 1956

There is no doubt that, until the Companies Act of 1956 came into operation, there was considerable concentration of control in the hands of a few managing agency firms. Even apart from the manipulation of funds of the managed companies by managing agents, a large proportion of the output of important national industries was controlled by one or a few agency houses, and this control enabled them to resort to monopolistic practices in determining outputs and prices. This power was further intensified when a managing agent controlled enterprises in various industries, some of which were vertically related. The extensive sphere of influence of managing agents resulted in a bias of the system towards financial manipulation and speculation in the stocks of the operating companies. The system also led to the concentration of entrepreneurial and financial resources in a small number of families which had entrenched themselves in most of the important industries.

Let us take a few instances: On the eve of World War II, 53 jute mills with a capital of Rs 18 crores, out of a total

of 100 mills with Rs 23 crores, were controlled by 17 managing agents. Four of them controlled as many as 30 mills. Out of a total of 247 coal companies with a capital of Rs 10 crores, 60 companies with a capital of Rs $6\frac{1}{4}$ crores were controlled by 18 firms. Four of them controlled, between themselves, 31 companies. In tea, 117 companies were controlled by 17 firms, and five of them controlled 74 companies. Similar concentration of control existed in sugar and other industries. In the cement industry, the Associated Cement Company took over the business of 11 different companies. The British India Corporation, formed in 1920, had a capital of Rs $1\frac{1}{4}$ crores with a single Board of Directors and controlled two woollen mills, one cotton mill, the biggest boot manufacturing company in the country and a company dealing in automobiles. In Western India, the Tatas alone controlled 22 concerns with a capital of roughly Rs 30 crores. These included four cotton mills, four power companies, an oil mill, an iron and steel factory, hotels, airways, chemical, and insurance companies—with total assets exceeding Rs 100 crores. Andrew Yule & Co. of Calcutta controlled 52 concerns with a capital of Rs 7 crores. 34 British Trusts controlled about 400 concerns with an approximate capital of Rs 75.5 crores, while half a dozen Indian Trusts controlled some 50 concerns with Rs 37.5 crores of capital.[1]

The above control was ultimately exercised, not by a few firms, but by a few individuals. In the jute industry, 132 persons were directors in 271 concerns. According to an unofficial survey, 500 important industrial companies were managed by 2,000 directors. At the apex of the pyramid stood ten men holding 300 directorships.[2] These firms maintained close connexion with banks and other financial institutions by the simple method of common directorships.

The tendency towards the process of concentration was further accelerated after World War II. The following figures are interesting:

[1] Reserve Bank of India, *Census of India's Foreign Liabilities and Assets*, Bombay 1950.

[2] The unofficial survey was carried out by Mr. Asoka Mehta of the Praja Socialist Party. Vide also P. A. Wadia and K. T. Merchant, *Our Economic Problem*, Bombay, 1960.

Number of companies managed by 6 managing agents in selected industries[1]

	1911	1931	1951	1956
Jute ..	22	31	38	40
Cotton ..	24	27	36	39
Sugar ..	6	9	30	32
Tea ..	58	84	86	100
Engineering ..	6	15	21	34

The true extent of the concentration of control could be gauged by the number of directorships enjoyed by a single individual. An analysis of the distribution of directorships reveals that a large number of directorships were held by a minority of influential persons. In the coal industry, out of 56 companies, 51 companies with 247 directorships were controlled by 28 persons, seven of whom held 64 directorships. In Jute, 267 directorships were held by 130 persons, four of whom had 82 directorships. In the joint-stock companies surveyed by Mr. Asoka Mehta, there were 3,728 directorships distributed among 1,103 persons: sixty-one of these persons held 1,038 directorships, (an average of 16 per person,) while twenty of them held 805 directorships (an average of 40).

According to another study (made by the Department of Company Law Administration), in 1954-55, 17 top agencies had each under its own management some 10 or more companies. They managed a total of 359 companies having an aggregate paid-up capital of Rs 114 crores, which was about one-fourth of the total paid-up capital of all companies under the managing agency system and about 12.5 per cent of the total in the entire corporate sector in that year. To this could be added extension of control through subsidiaries of companies and interlocking of directorates.

A study made by the National Council of Applied Economic Research (this related to the year 1956), in four selected industries (cotton textiles, jute, tea and sugar) controlled by the three largest managing agencies in each industry gave the following picture:

[1] These figures have been compiled from the relevant editions of the *Investors' India Year Book* published by Messrs. Place, Siddons & Gough of Calcutta.

Percentage of the Corporate Sector controlled by Three Largest Managing Agencies

Industry		*Total no. of cos.*	*No. of cos. under 3 largest agencies*	*Percentage of paid-up capital*	*Percentage of net fixed assets*	*Percentage of total assets*
Cotton Textiles	..	213	13	14.7	19.0	16.3
Jute	..	62	23	27.0	31.7	28.3
Tea	..	155	47	25.5	18.9	25.4
Sugar	..	81	15	21.0	18.5	20.7

The Position Today

What is the position today? Is concentration of control on the increase or on the decrease? No analysis has been made of the present state of affairs by either the Department of Company Law Administration or the National Council of Applied Economic Research and as such it is difficult to give a categorical answer.

Certain facts and circumstances can, however, be noted. As a result of the restrictions and regulations imposed by the Companies Act of 1956, managing agency firms no longer have the undisputed sway they once had. We have already seen that most of the new promotions of companies are outside the managing agency system. Devices of various kinds which could be pursued with impunity prior to 1956 are no longer permissible.[1]

On the other hand, simply because the managing agency system is under control, it does not necessarily follow that there is no concentration of economic power. As we have seen, concentration is a common feature of many countries in the West. 'The problem, as it is chiefly represented today, arises from the dominant position occupied in key industrial areas by giant corporations, singly or in small groups—the rule of oligopoly.'

This kind of concentration is to be found in India also. Industrial enterprise in India today appears to be concentrated more and more in a few groups or individuals. The

[1] Speaking on the Companies (Amendment) Bill, 1959, in the *Lok Sabha* on 18 November 1960, Mr. Lal Bahadur Shastri, Minister of Commerce and Industry said: 'The number of managing agencies controlling more than 10 companies are very few. Over 84 per cent of the managing agencies do not control more than one company.'

Tatas now have sole or majority control in 53 companies, the House of Birlas in 333 companies, the J.K. Industries Group in some 60 companies, and the Walchands in 16 companies. According to some, control is now passing into the hands of a few combines, because there does not exist in India today those 'countervailing powers' of a strong trade unionism or of buyers' groups which regulate or moderate an economy like that of the U.S.A. The development of 'countervailing power' requires a certain minimum opportunity and capacity for organisation amongst those who are the victims of the 'original power' of monopolistic capitalism: in India, it is argued, neither the shareholders nor the consumers have the necessary opportunity or capacity.[1]

In India today, the State has stepped in as the 'countervailing power'. The Government has already got in its armoury a number of measures that can be, and are, employed to check concentration of economic power. These include the Tariff Act, the Industries (Development and Regulation) Act, the Capital Issues Control and the Companies Act itself. Moreover, the basic industrial policy of Government is to widen the public sector and thereby reduce the power of the private sector.

Among the conditions that are necessary for preventing undue concentration of power in any industrial group, two are of special importance. Firstly, there should be no combination among the larger units and, secondly, there should not be any serious impediment to the entry of new enterprises. Both these conditions are to be found in India today. There is keen competition among the companies in the same industry, whether they are managed by managing agents or Boards of Directors. There has been no evidence of collusive combinations among them to restrict output or to raise prices. Even on the rare occasions when output has shown a tendency to fall, or prices a tendency to rise, owing to the operation of factors over which industry has no control (e.g. shortage of raw materials or levy of heavy excise duties), the Government has appeared on the scene and sometimes compelled

[1] For a brilliant exposition of the concept of 'countervailing power' in the economic system, the reader is referred to J. K. Galbraith, *American Capitalism*, New York, 1958.

the industries concerned to get on with production and distribution even at a temporary loss. As regards the entry of new enterprises, not only do existing industrial groups have no powers to stop new entrants, but they submit gracefully to any measure Government takes to broaden the industrial base.

As regards market power, the scope for concentration is even less. The prices of important commodities like steel, cement, coal, petroleum and sugar are more or less fixed by Government, while even in regard to others, a careful watch is kept. Although temporary cornering of goods and services is not unknown, restrictive practices deliberately manipulating prices are few and far between.

Another fact which militates against concentration of economic power in a few individuals or groups is the deliberate encouragement given by Government to small entrepreneurs. A sum of Rs 33.6 crores was spent by Government on the development of cottage and small-scale industries in the First Plan and Rs 180 crores in the Second Plan. A provision of Rs 250 crores on this account has been made in the Third Plan. In addition, small industries get financial accommodation from the various specialised institutions set up by Government; some of them are also given preference while tendering for Government institutions and projects. India is certainly humming with industrial activity today, but this activity is not confined to a privileged few.

Nevertheless, it would be unwise to overlook certain signs on the economic horizon. The very fact of rapid economic growth has led to the emergence of a managerial-*cum*-entrepreneurial class drawing high salaries and emoluments—a kind of power élite—who almost live apart from the rest of the community. This rise of the U-sector has accentuated rather than reduced inequalities of income and wealth. This sector appears to be wielding a not inconsiderable amount of political power behind the scenes. It is such extra-economic consequences of the concentration of economic power as are really dangerous.[1]

[1] Vide the author's article entitled '*The Economic Position of the Average Indian Today*' published in the Golden Jubilee Number (1961) of *Commerce*, Bombay. Regarding the power exercised by this 'tightly knit and basically irresponsible' groups of men, in the U.S.A., the reader is referred to C. Wright Mills, *The Power Elite*, New York, 1957.

A recent study of the inter-corporate investments of five groups of companies (the Tatas, the Birlas, the Mafatlals, the Walchands and the Mahindras) also shows that, in some cases at least, control is being exercised by a small, well-knit corporate group.[1] This was achieved, not through the managing agency system (although nearly every group maintains a number of managing agencies), but through a system of integrated investments. Although individual shareholders held 52.5 per cent of the total value of equity shares and 50.7 per cent of the total value of preference shares in the companies managed by these five groups, Indian companies or firms accounted for 37.3 and 25.0 per cent of these two categories of shares. The following table shows the position at a glance:

Percentage Distribution of the Value of Shares in the Companies managed by the five Groups

(*Position as in* 1958)

	Equity Shares	*Preference Shares*
Indian Companies ..	37.3	25.0
Foreign Companies ..	2.6	0.6
L. I. C. ..	3.2	8.8
Government ..	1.2	10.4
Trusts ..	3.2	4.5
Indian Individuals ..	51.8	50.4
Individuals abroad ..	0.7	0.3
Total	100.0	100.0

The total share capital of the 491 companies covered in the above study was Rs 203.6 crores, out of which Rs 71.3 crores were held by Indian companies. A detailed break-up of this latter holding shows that Investment and Managing Agency companies of the Groups concerned were the biggest holders, providing Rs 38.1 crores. They are followed by Banks and Insurance (mostly the former, on behalf of their clients), with Rs 15.7 crores. Industrial Companies held Rs 15 crores, and the remaining Rs 2.5 crores came from Trading Companies, most of which were actually Investment Companies. The following table is relevant:

[1] The study was made by Dr. R. K. Hazari under the auspices of the Planning Commission. The preliminary results were published in a series of three articles in the *Economic Weekly*, Bombay, dated 26 November, 3 December and 10 December, 1960. The data which follow are taken from Dr. Hazari's study.

Synoptic View of the Inter-Corporate Holdings of 491 *Companies*

(*Position as in* 1958)

		Rs Crores
Total Share Capital	..	203.6
Holding of Indian Companies	..	71.3
Of which held by:		
Investment and Managing Agency Companies	..	38.1
Banks and Insurance	..	15.7
Industrial Companies	..	15.0
Trading Companies	..	2.5

A further analysis of the data relating to the 402 companies within the 'inner circle' of the five groups referred to above is even more revealing. Out of the total share capital of Rs 155 crores, the Controlling Groups provided Rs 63 crores or 40 per cent. Excluding the Tata Group, in which controlling blocks are very low in proportionate terms, the remaining four Controlling Groups provided Rs 45 crores or 57 per cent of the total share capital of Rs 79 crores. Even in regard to individual share-holdings, it is doubtful if they are as widespread as is sometimes asserted. A closer examination may show that quite a large number of the individual share-holdings are also held by the members of a particular Group or their friends.

The techniques of control vary from Group to Group, but there is no doubt that there is a tendency towards concentration. This large increase in inter-corporate investment has been caused, at least in part, by the high rates of taxation of *personal* income and wealth: the rich have sought the obvious way out, viz. to disperse and impersonalise their holdings of wealth, through the creation of companies and Trusts, as the latter enjoy a number of advantages ranging from comparatively low or no taxation at all to independent and perpetual existence.

Inter-corporate investment is not inherently anti-social. It provides a flexible mechanism for the control of existing undertakings and promotion of new enterprises. The danger, however, lies in the fact that it enables controlling interests to maximise their area of control and influence through a chain of minimum and indirect investments. The State has, therefore, to step in to prevent abuses which may be detri-

mental to the interests of shareholders and even more to the economic development of the country.[1]

An interesting point to be noted in this connection is that, unlike in many companies in the West, the integration these groups seek to achieve is basically not technical, but financial and managerial. The propensity is more to spread investments pretty far and wide than to secure economies of production and distribution. 'The interests of these Groups are far too diffused over industrial as well as non-industrial occupations to enable—and induce—them to concentrate their attention on the problems of individual industries.'[2]

We should not, however, be carried away by passions and prejudices. We should look at the problem objectively and dispassionately. That there is scope for concentration of control is an undisputed fact, but is this not inevitable in the modern world? Leaving aside the U.S.A., the land of giant combines and Trusts, do we not find the same trend in the U.K., France, Germany, Italy, Japan and even in the U.S.S.R.? In a world in which the traditional sources of power bid fair to be replaced by atomic energy, in which automation is percolating into most manufacturing industries, it would be foolish to deplore the emergence of big industrial units.[3] The really important question is whether these big units can be made to serve the interests of the common people. If the State can ensure this, one need not be unduly worried by the mere size of a unit nor even by the fact that power sometimes rests with a few individuals or groups.

[1] The recent amendment of the Companies Act is expected to prevent such abuses, but the present writer is not sure if it would curb 'concentration of control'.

[2] In fairness to them, it must be added that there are two specific reasons for this tendency to proliferate into unrelated industries. They are (*a*) the fear of nationalisation of basic industries in which certain groups, like the Tatas, have invested the bulk of their capital, management and prestige; and (*b*) the absence at times of an adequately gainful outlet within their occupation for the surplus funds that accumulate in some of the older concerns.

[3] Although not strictly relevant, it is interesting to record that, according to statement made in the *Lok Sabha* on 29 November 1960, by Mr. K. Gopala Reddy, Union Minister for Revenue and Expenditure, the number of 'millionaires' among non-company wealth tax assessees, owning property worth over a crore of rupees, was only 24 on 31 March 1960. This was in addition to 16 millionaires among feudal aristocrats. Vide *The Statesman*, New Delhi, 1 December 1960.

Chapter X

SOME ANCILLARY FACETS OF INDUSTRIAL ENTERPRISE IN INDIA

Growth of Private Limited Companies

An interesting feature in the development of industrial enterprise in India is the rapid growth of private limited companies (as distinguished from public limited ones). Historically, the distinction between a private limited company and a public limited company arose as follows: As corporate enterprise was increasingly utilised in the field of medium- and small-scale business, the need was felt for some relaxation in the legal requirements applicable to the formation and management of companies. The initiative was taken by Germany in 1892 in relaxing the provisions applicable to private companies by dispensing with the issue of share certificates. Also, a simpler method of management was provided and the filing of, and publicity for, accounts were dispensed with. This mode of distinction was adopted by a number of countries on the Continent. In the U. K., however, it was the Companies Act of 1907 which for the first time made a distinction between private and public companies by exempting private companies from the obligations to file balance sheets with the Registrar of Companies. It also imposed certain conditions as to membership and restrictions on transfer, and the inviting of public subscription for their shares was forbidden.

Under the Indian Companies Act of 1913, a company was deemed to be a private company if, in its articles, it (*a*) restricted the right to transfer its shares, (*b*) limited the number of its members to fifty only (excluding employees) and (*c*) prohibited any invitation to the public to subscribe for any shares or debentures of the Company. These restrictions, limitations and prohibitions must be continued to be observed by a private company during its existence: otherwise, it will cease to enjoy the privileges and exemptions conferred by the Act.

A private company thus enjoyed certain privileges and

exemptions, the most essential and valuable of which was the one relating to the exemption from the filing of the balance sheet and the profit and loss account with the Registrar. This concession by itself was responsible for the promotion of numerous private companies in the U.K. and, in that country, private companies now outnumber public companies by more than twenty to one.

Although the proportion of private to public companies in India is nowhere like what it is in the U.K., there has been a rapid growth in the number of private companies since 1919-20.[1] During this year, the percentage of private to all companies (public as well as private) was 18·2. This gradually increased to 47·3 in 1938-39 and the figure in 1960-61 was 74·1. As a matter of fact, more private than public companies have been functioning in this country since the end of World War II.

As regards paid-up capital, although the total paid-up capital of private companies is still less than the total paid-up capital of public companies, there has been a progressive increase in the relative percentage of the paid-up capital of private and public companies. While in 1919-20, the paid-up capital of private companies constituted only 15 per cent of the total paid-up capital of all companies, the corresponding figure in 1960-61 was 49 per cent.

As has been stated already, the rapid growth of private companies was largely due, both in the U.K. and India, to the privileges and exemptions which they enjoyed under the law. A private company offered a convenient method for converting a proprietary business into the joint-stock form of organisation so that all the advantages of company incorporation might be derived. These were (*a*) limited liability for the members, (*b*) corporate personality for the business, (*c*) continuity of existence in spite of changes in membership, and (*d*) division of financial ownership into two or more classes of shareholders with different rights as to profits, voting powers, etc. In the U.K., the very large number of private companies was due to the conversion of many 'family businesses' into the joint-stock form of organisation. It may also be added that private companies continued to grow

[1] *Vide* Appendix VII.

because of certain characteristics of human nature. There were many people who wanted to manage their own concerns themselves and at the same time required the assistance of a few outsiders to get the requisite capital: the obvious course for such people was to form a private company.

What is striking in the case of India is not the large relative proportion of private companies to all joint-stock companies, but the *rate* of increase of this proportion. Notwithstanding the need for larger capital in the floatation of industry, the number of private companies has been increasing faster than the number of public companies. Apart from the general reasons, there have been three special factors favouring the growth of private companies in India. Firstly, managing agency concerns which were composed of persons who were either relatives or close business associates found it convenient, from many points of view, to convert their firms into private limited companies. Secondly, until lately, the investment market was more or less unresponsive to a general appeal for the public subscription of shares. Hence entrepreneurs often preferred to start their business as private companies, especially as they knew that it was always possible to convert a private company into a public one. Finally, the restrictions imposed by the Amending Act of 1936 on all public companies (private companies were exempted from many of them) induced many a shrewd entrepreneur to organise his business as a private company rather than as a public one.

An interesting feature of the private companies operating in India is that a large number of shareholders hold 50 per cent or more of shares. This was revealed in a sample analysis carried out by the Taxation Enquiry Commission, on data supplied by the Income Tax Department of the Government of India.

The distinction in the nature of the obligations to which public and private companies are subject, was maintained in the Companies Act of 1956, but it was provided that the balance sheet and the profit and loss account of a private limited company should also be audited by qualified auditors and that copies of the balance sheets, certified as true copies by the Company's auditors, together with the auditor's report, should be filed with the Registrar. Under the recent

Companies Amendment Act of 1960, private companies also are required to file profit and loss accounts separately.

During 1955-56, just preceding the year of enforcement of the Companies Act of 1956, and for a couple of years thereafter, there was an appreciable increase in the number of private companies, mainly because the belief persisted that such companies would escape some of the rigorous provisions of the Act. Under this belief, a large number of public companies were converted into private companies, but the process was halted from 1957-58 onwards.[1] Even so, on 31 March 1956, the ratio of private to public companies was 2:1; five years later, i.e. on 31 March 1961, the ratio was 2·8:1. The ratio of the paid-up capital of private to public companies was 1:2 in 1955-56; it was 1:1 in 1960-61. It may be mentioned, however, that an important factor which turned the scales in favour of private companies was the Rs 300 crores paid-up capital of the Hindustan Steel, Ltd., which was set up as a private company in the public sector. A few other big-sized Government companies were also registered during the period 1956-61 as private companies.

This trend in the growth of private companies (relative to public companies) is not likely to be maintained, as it is being increasingly realised that almost the same types of restrictions apply to both private and public companies.

Private Companies treated Public Companies

As stated already, the Act of 1936 introduced, for the first time, a distinction between private companies which were subsidiaries of public companies and those which were not. The first category was equated with public companies. While some privileges like commencing business without minimum subscription and not holding the statutory meeting could be enjoyed by all private companies, other privileges like non-adherence to the ceiling on managerial remuneration, setting of an age limit for directors, granting of loans to directors,

[1] The 'Third Annual Report' on the working and administration of the Companies Act of 1956 stated as follows: 'The number of conversion (of public companies into private companies) in 1956-57 was abnormally high, largely because of exaggerated fears as to the nature of some of the restrictive provisions of the Act applicable to public companies. With increasing knowledge and appreciation of the manner in which the new Act was being administered, these fears largely disappeared.'

to give a few examples, could be enjoyed only by private companies which were not subsidiaries of public companies under the Companies Act of 1956.

The principle of treating certain categories of private companies as public companies was carried a step further by the latest Companies Amendment Act of 1960. The new section 43A introduced by the above Act provides that, where not less than twenty-five per cent of the paid-up capital of a private company is held by one or more companies, private or public, Indian or foreign, the private company becomes a public company, subject to certain exceptions. The exceptions are (i) where the entire paid-up capital is held by another single Indian private company or by one or more foreign companies, private or public, or (ii) where the capital is held by one or more Indian private companies, provided no company is a shareholder in any of such shareholding companies, and the total number of members of the shareholding companies and the private company in which shares are held, does not exceed fifty.

Company Failures

Although the number of joint-stock companies has increased steadily since the beginning of the present century, it is interesting to note that, between 1921 and 1935, the paid-up capital did not register much of an increase. This was due to the fact that during this period there occurred a very large number of company failures, with the result that the Indian investor, habitually shy, became shyer still. Between 1936 and 1951, the number of liquidations varied between 288 in 1942-43 and 1,167 in 1949-50. The paid-up capital involved also ranged from Rs 3.3 crores to Rs 12.1 crores per annum. These variations do not, however, point to any significant moral, except that liquidations continued within a certain range.

Since 1951-52, the number of liquidations has been again on the increase, although the paid-up capital involved shows considerable fluctuations. It may be pointed out, however, that the figures from 1956-57 onwards include a very large number of companies which were moribund rather than bad. According to the Department of Company Law Administration, out of 9,386 companies that ceased to work during

1956-61, more than 7,000 (i.e. about 80%) were struck off the register under Section 560 of the Companies Act in pursuance of a vigorous policy of weeding out virtually defunct companies.

Causes of Company Failures

The position is, however, alarming enough to demand close scrutiny. Why is it that such a large number of companies still continue to fail in our country?

According to a famous writer on business management, the causes of joint-stock company failures can be broadly divided into two classes: (*a*) those operating from outside and (*b*) those operating from inside. To the former class belong such causes as competition, change in the demand for the products of the company, operation of the business cycle and normal casualties. In the latter class lie such causes as archaic methods of production, slowness of collections, unwise distribution of cash dividends, incompetent sales organisation, high operating expenses, over-capitalization, excessive floating debt, failure to make adequate provision for depreciation, and fraud. According to the same writer, all these causes are ultimately due to 'incompetence'; inside causes are, of course, obviously signs of 'incompetence', but even outside causes may be said to be due to 'incompetence', because with good management, the evil effects of most of these causes can be modified even if the causes themselves cannot be humanly avoided.[1]

Now, in India, owing to the fact that for a long time industrial and economic policy was not completely in the hands of ministers responsible to the legislature, there was a tendency to exaggerate the outside causes and to minimise the inside ones. An impartial study of some of these industrial failures would, however, show that, in the majority of cases, they were what Gerstenberg would call the 'results of incompetence and fraud'. Floatation by numerous adventurers of companies which were inevitably closed down within a few years of their inception not only entailed a loss involving crores of rupees to the unwary investors, but acted as a hindrance to the commercial and industrial development of the country

[1] C. W. Gerstenberg, *Financial Organisation and Management*, New York, 1954.

by joint-stock enterprise. To put it bluntly, in India depraved business morality perhaps accounted for the largest number of company failures. The old company law left several loopholes for unscrupulous promoters, and the shareholders had no protection against their actions unless these were found to be within the orbit of criminal breach of trust.

Next to fraud, the most important cause of failures has been incompetence or inefficiency in the strict sense of the term. Very often, bona fide floatations launched with the best intentions and enthusiasm came to grief because their prospects and possibilities had not been carefully scrutinized. In one way in particular, the law connived at this form of incompetence, at least till 1936. The law left the determination of the minimum capital with which to start business practically to the discretion of the promoters, subject only to the condition that the certificate for commencement of business should be issued on prior realization of 5 per cent of the subscribed capital as the application money. But as this percentage very often proved far too short of the capital required even for the acquisition of lands and the construction of buildings and factory, the provision failed to afford any assurance that the company had attained the actual working stage. Numerous cases occurred in which, despite serious efforts to procure sufficient funds by disposing of its shares, a company failed to secure any substantial amount in excess of the statutory minimum, with the result that the company had to be closed down after the little money it had procured from its sale of shares had been spent in sundry preliminary expenses.

The Amending Act of 1936 introduced a number of safeguards to deal with mushroom and fraudulent companies. For example, it required that the minimum subscription (on which alone certificates of commencement of business could be obtained from the Registrar of Joint-Stock Companies) should be fixed by the directors upon a certain specified basis. The directors were to provide for (*a*) the purchase price of any property to be purchased out of the proceeds of the issue of shares, (*b*) the preliminary expenses, (*c*) commission for procuring shares, (*d*) moneys borrowed by the company in respect of the preceding matters, and (*e*) working capital

all of which meant that the minimum subscription had to be such as to provide not only for the acquisition of the necessities for the business to be carried on by the company, but also for the working capital. Again, while under the old Act there was nothing to prevent a company from utilizing moneys received from prospective shareholders even before shares were allotted to them, it was no longer possible under the Amending Act to do so. All such moneys were to be kept away from the reach of the company and its promoters, and to be kept deposited in a scheduled bank until a certificate of commencement of business had been obtained.

In the matter of fraudulent companies, until 1939, apart from the ordinary remedy available under the Indian criminal law, there was really no provision for the investigation and detection of frauds practised by some of the companies on the public. The Amending Act removed this omission and authorized the Registrar of Joint-Stock Companies to investigate cases of fraud brought to his notice. He could make an enquiry and report to the local Government which might, at the cost of the State, order the prosecution of persons who were believed to be guilty of an offence in relation to the company. Any officer or director of the company who was convicted as a result of such prosecution was debarred, unless permitted by the court, from directly taking part in the management of a company for a period of five years.

As we have seen, even these safeguards were not able to bring down the number of company failures in this country. It is not known how many of the failures in recent years were caused by deliberate fraud and how many by inefficiency or incompetence, but the fact remains that considerable sums of money which could and should have been profitably utilised for development, have been lost to the country. The various safeguards provided under the Act of 1956 have, however, put some brake on company failures caused by deliberate fraud.

Chapter XI

PROBLEMS OF MANAGEMENT

Importance of Management

As noted already, until even a decade ago, lack of finance and the absence of dynamic entrepreneurship were considered to be the main impediments in the path of accelerated industrial development. Lack of finance has long ceased to be a cause for worry. As regards entrepreneurship, while it might not have been 'dynamic', even in pre-1947 India there was no dearth of persons prepared to take the necessary risks in starting new ventures. We have already noted the part played by managing agents in promoting industrial development. Even outside the old managing houses, there were men of vision who pioneered new undertakings in the face of tremendous odds and who now have an honoured place in the industrial history of our country.

Entrepreneurship, however, provides only the initial stimulus. Much more important is the building up of an organisation to run an undertaking. 'Organisation is a broader concept than entrepreneurship. It connotes a constellation of functions including specifically the management of risk and uncertainty, planning and innovation, co-ordination, administration and control, and routine supervision of the enterprise. It connotes also the integrated hierarchy of the persons who are primarily concerned with exercise of these functions, viz. the management.'[1]

The importance of the management has greatly increased owing to the fact that business itself has become vast, complicated and long-term. It is no longer possible for the shareholders or even their representatives on the Board of Directors to 'manage' a modern industrial undertaking effectively. The task has to be entrusted to skilled and qualified executives, who possess the necessary drive, initiative, imagination and power of co-ordination. It is for the management to build up a coherent structure and an integrated system of

[1] 'Management' is a collective title for a group of men occupying a certain status in the hierarchy of a business undertaking.

inter-communication, with inter-relationships between the diverse elements which enter into production and exchange, so that the wheels of industry may be kept continually on the move. In all the industrially advanced countries, management has become a new and exacting profession. 'Managing a business is not just a matter of hunch or native ability.... The manager can, and is expected to, improve his performance in all areas of management through the systematic study of principles, the acquisition of organised knowledge and the systematic analysis of his own performance in all areas of his work and job and on all levels of management.' In other words, in the competitive world today, the progress of a business undertaking depends very largely on the men that are selected to manage it.

Development of Management Personnel in India

It is only lately that modern methods of management are being adopted in our country in replacement of old methods. The growing complexities of the unprecedented advances made in science and technology have brought in their train problems which cannot be tackled adequately by the old types of managers. Business enterprise no longer consists in merely finding the money or launching a project. The successful business man has to cope not only with the problems of assembling and making the most effective use of the physical resources, but to integrate the work of a variety of specialists and men each of whom is important in his own field or area of work. The complexities of the Company Law and the need to conform to the policies formulated and laid down by the State have also brought about a situation in which the actual management has to be entrusted to persons who can manage in the true sense of the term.

Even in the most developed countries, however, good and efficient managers are not very plentiful. It is not to be wondered, therefore, that India has got only a handful of such men. But the leeway is being made up. In the organised corporate sector, increasing reliance is being placed on qualified personnel—persons having knowledge of cost accountancy, business administration and/or personnel management. On the one hand, various refresher courses and seminars are

being organised to reshape talent already available in business. On the other hand, young men with the right outlook are being recruited to the junior grades of management, in the hope that, in course of time, they would be able to fill in the top management positions which are now occupied by non-Indians. Even in colleges and universities, courses in business administration are becoming increasingly popular and many business firms are sending their staff to take such courses. An Administrative Staff Training College for developing managerial talent has been functioning at Hyderabad for quite some time now. Staff training colleges on individual and collective basis are also being set up in different banking, commercial and industrial establishments in different parts of the country.

In the bigger undertakings, the process of modernisation in thought and approach is going on apace. There is active and organised thinking on the internal problems of establishments, the accent being on how to achieve greater efficiency and higher productivity. A National Productivity Council has also been set up at New Delhi, with a network of Local Productivity Councils at almost every important business centre in the country.

As a consequence, the old familiar Indian business magnate, functioning more or less on a personal level, is being replaced by managers and executives functioning on an institutional basis. As stated already, to a large extent, this change has been forced upon the corporate sector by the imperative logic of circumstances. Snap personal decisions or the thinking of a mere financier are incapable of meeting the organisational needs of modern industry, which calls increasingly for the adoption of 'scientific' methods in the administrative field as well. A study conducted by the UNESCO Research Centre at Calcutta (since shifted to New Delhi) gives a graphic account of this transformation over the last decade at two business centres, viz. Bombay and Calcutta. It indicates how, even in undertakings financed largely by a family or a group, the top and middle executives are now being selected on the basis of capacity and skill and not on the basis of their connection with the investor or entrepreneur.

A Word of Caution

A note of warning, may, however, be sounded here. Of late, there has been a tendency to treat the management profession as something like the sacred preserve of an élite. An aura of mystery seems to surround some of the top business executives. They speak pedantically of the intricacies of the problems of management, giving the outsider the impression that it is a difficult art which can be acquired only by a select few. 'A good manager,' it is urged, 'has to be a great genius.'

Now, while it is not denied that, in the complex conditions of business today, a good manager must combine within himself a number of rare qualities, none of these are such as cannot be acquired by a person with the necessary flexibility of mind. Too much stress should not also be laid on the 'organisational' aspect of the modern business. As has been brilliantly put in by William H. Whyte, 'precisely because it *is* an age of organisation, it is the other side of the coin that needs emphasis. In our anxiety to make the organisation work, we have come close to deifying it. This is bad for the organisation. It is worse for the individual. In soothing him, it robs him of the intellectual armour he so badly needs. The individual must assert himself against the organisation which tries to swallow him up.'[1]

Obligations of Good Management

Another point to be noted is that, apart from professional skill, the management should live up to an ethical code of conduct. While the first obligation of the management is to the proprietor or the shareholder, he owes certain obligations to the employee, the consumer and the State as well. 'The benefits extended to the employee must not be a matter of mere philanthropy, but an obligation, on the ground that he is as much entitled to good life as anyone else, He is, therefore, entitled to fair wages, and to security. He is entitled to reasonably pleasant conditions of work and to have recreational facility and opportunity. He is entitled to have opportunities for advancement. If the business cannot carry him

[1] For a brilliant analysis of this dangerous trend in modern American society which some of us in India are trying to copy, the reader is referred to William H. Whyte, Jr., *The Organisation Man*, New York, 1959.

on the pay-roll, the employee is entitled to compensation and retrenchment benefits, so that he can absorb the shock before he moves on to some other job. He is also entitled to some security after retirement. All these have now assumed the place of an obligation of good business management and are no longer things which one doles out as mere items of cost in balancing the profit and loss account on the right side.'[1]

As regards the obligation to the consumer, modern management must recognise that the consumer is entitled to get fair quality goods, in full measure and at a fair price. Profiteering is a direct violation of this particular canon of the code of business ethics.

Finally, good management must be actively aware of its obligation towards the State. This obligations does not end with the payment of taxes. It extends to (*a*) assisting the Government with advice, guidance and even constructive criticism in the formulation of a policy, but (*b*) carrying out the Government policy faithfully, once it has been formulated and laid down.

It must be stated here with regret that there are not many managements in our country today which live up to these high obligations. To the extent that they do not, they put a brake on orderly economic development. It does not ultimately help private business enterprise if the State has to intervene on behalf of the employee or the consumer. As has been aptly put by a distinguished member of the top management, 'if free enterprise is to actively survive in India, it can only do so on the strength of the contribution it makes to the common good.'[2]

[1] Vide the essay entitled '*Ethics in Company Management*' by Mr. N. Dandekar in '*The Role of Joint Stock Companies in India's Economic Progress*', published by the Forum of Free Enterprise, Bombay, 1959.
[2] N. Dandekar, *op. cit.*

CHAPTER XII

COMPANY FINANCES AND PROFITS

Introductory

A CONTEMPORARY PHENOMENON noticed in all important industrially developed countries is the growing importance of retained profits, accumulated reserves, and depreciation allowances as a source of finance for industrial development. In India also, over the last decade, these 'internal finances' have become one of the major components of the total funds made available to the companies.[1] Incentives are being provided through fiscal devices so that accumulated profits are not frittered away, but re-invested in the business.

It should be noted, however, that this source of finance is beyond the reach of new companies or those that are passing through teething troubles. It is available only to companies in a sound position and to those which have been in operation for a fairly long time.

Another point to be noted is that the internal finances of a company are not available to other companies. If such funds were deposited with banks or investment companies, these could have been invested by the latter in other companies. Retained profits thus result in the withholding of substantial funds from the public capital market.

Trend in Internal Financing

Some light on this subject of 'internal financing' is thrown by four studies of company finances made by the Reserve Bank of India. The first study was made in 1957 in respect of 750 companies which represented 66% of the total paid-up capital of all public companies at work. According to this study, during the years 1950-55, internal sources contributed Rs 265 crores or nearly 60 per cent of the total funds made available to these companies.[2]

[1] This may be contrasted with the period prior to 1947, when despite substantial profits having been made, many companies dissipated a considerable portion thereof by declaring very high dividends and embarking on ancillary schemes of doubtful economic value.

[2] *Reserve Bank of India Bulletin*, September 1957.

The second study was made in 1958 in respect of 1,001 companies, representing 76% of the total paid-up capital of all companies at work during the year 1957. This study placed internal sources at Rs 65.8 crores or 27.7 per cent of the total funds that became available to the companies.[1]

The third study was made in 1960, also in respect of 1,001 companies and for the year 1958. According to this study, internal resources accounted for Rs 77.7 crores or 48.5 per cent of the total funds.[2]

The fourth study took place in 1960 and related to the year 1959. This study reveals that internal resources (Rs. 99.7 crores) constituted 63 per cent of the total funds.[3]

While too much significance should not be attached to these fluctuations from year to year (the position is affected by facts and situations in particular industries in a particular year), it is obvious that internal resources are becoming more and more important in the matter of financing of industry.

Trend in Capital and Debenture Issues

The Reserve Bank studies referred to above also give a bird's-eye view of recent trends in the issue of shares and debentures. For instance, new issues of shares and debentures in 1959 were Rs. 32.4 crores as against Rs. 29.1 crores in 1957 and Rs. 27.8 crores in 1958. As a percentage of total issues, ordinary shares declined in importance, the percentage falling from 75.7 per cent in 1956 to 62.0 per cent in 1959. Preference shares, on the other hand, showed a marked improvement and amounted to 22.5 per cent of the total issues in 1959 as against 14.2 per cent in 1958. Debentures, however, declined from 21.3 per cent of the total in 1958 to 15.5 per cent in 1959. Over three-fifths of the debenture issues were in the aluminium industry alone, while about three-fifths of the preference shares were accounted for by the iron and steel and engineering industries. The rate of interest offered on debentures ranged between $5\frac{1}{2}$ and 7 per cent.

[1] *Reserve Bank of India Bulletin*, August 1959.
[2] *op. cit.* September 1960.
[3] *op. cit.* September 1961.

According to a further study made by the Reserve Bank of India, a feature in recent years has been the growing importance of 'initial' issues, i.e. capital issues by *new* companies, as compared to 'further' issues, i.e. capital issues by *existing* companies. The proportion of 'initial' issues to total issues rose from 8 per cent in 1956 to 28 per cent in 1960, and, in the period January-June, 1960, it was as high as 59 per cent.

During the entire period January 1956 to June 1960, out of the 314 new issues amounting to Rs 171 crores, 72 per cent or 211 issues were in ordinary shares, 17 per cent or 76 issues in preference shares and 11 per cent or 27 issues in debentures. Then again, of the 211 ordinary share issues for Rs 123 crores, as much as Rs 57.81 crores or 47 per cent was by 10 giant companies.[1]

Trend in Borrowings

One thing which has been very noticeable in recent years is the shift in emphasis from shareholders' capital to a much greater reliance on borrowed capital.[2] This calls for a high degree of vigilance on the part of the management, as borrowings involve definite commitment for repayment of capital and interest. Before a company decides to borrow, it must carefully examine its ability to repay the borrowings as and when they become due, besides meeting a the periodic payments of interest. On the other hand, if everything goes well, larger reliance on borrowing may even be of advantage to the equity shareholder, inasmuch as the interest payable on borrowings tends to be less and the residuary profits come to the shareholder in the shape of higher dividend on equity shares. It also increases the chances of capital appreciation.

Sources and Uses of Funds

In an admirable study just published by the Research & Statistics Division of the Department of Company Law Administration, a comparative picture has been given of the overall position of sources and uses of funds during the First

[1] *Reserve Bank of India Bulletin*, February 1961.

[2] According to a study made by the Reserve Bank of India of 1,001 companies, their owned resources (i.e. paid-up capital plus free reserves and surplus) as a percentage of the total capital employed, declined from 52 per cent in 1955 to 47 per cent in 1959.

Plan period and the first two years of the Second Plan period.[1] The estimated increase in the total resources of the companies over the seven-year period 1951-57, comes to Rs 1,321 crores, made up of Rs 710 crores under the external heads and Rs 611 crores under the internal heads. During 1956 and 1957, there was a clear shift in favour of the external sources—brought about by a phenomenal rise in the borrowings from banks.

As regards the use of funds, the building up of gross fixed assets has been going on continuously without any break since 1951. This affords a proof of the increasing tempo of industrial activity in the country. The company inventories have also been rising since 1954. The share of inventories has, however, remained more or less steady at around 29% to 32% of the total net fixed assets.

Changes in Costs

A very interesting analysis of changes in costs has been made by the Research Division of the Indian Institute of Public Opinion, New Delhi. The basic data were obtained from the Reserve Bank of India studies referred to earlier in this chapter, but in view of the differences in the samples for the periods 1950-54 and 1955-58, the figures from 1950 to 1954 for 750 companies were 'blown up', using the co-efficient for 1955 as between the 750 companies and the 1,001 companies.[2]

This analysis reveals that, contrary to popular belief, manufacturing expenses *as a percentage of income* dropped steadily between 1950 and 1958. The figure was 56.35 in 1950, 51.42 in 1955 and 48.39 in 1958. Even in the group of salaries and wages, the figures were 14.89, 14.41 and 13.82 respectively. A similar, but less noticeable, trend could be seen in 'inventories' as a percentage of sales: these were 34.48 in 1950, 30.10 in 1955 and 31.63 in 1958. It is evident that the principle of increasing returns has been in operation since 1950.

The net assets of all the major industries at 'current' rupees had also risen from Rs 326.65 crores in 1950 to Rs 351.81 crores in 1958. There is no year in which this trend was

[1] Vide Raj K. Nigam and N. D. Joshi, *Trends in Company Finances with particular reference to the First and Second Plan Periods*, New Delhi, 1961.

[2] *Quarterly Economic Report* No. 26 of the Indian Institute of Public Opinion, New Delhi, October 1960.

reversed. On the other hand, there has been a very substantial change in the *rate* of rise, which was moderate between 1950 and 1953 and then gradually got stepped up and rose to nearly Rs 100 crores additional a year from 1954 to 1958. Company incomes also rose from Rs 1149.56 crores in 1950 to Rs 2082.21 crores in 1958. This is as it should have been, as the benefits of increasing returns can be seen only when investment begins to 'fructify'.

Company Profits

In recent years, a good deal of criticism has been levelled at the alleged usurpation of huge profits by most companies—to the detriment of the long-term interests of industry. The Planning Commission, for instance, referred in their First Five-Year Plan to the 'arrears in replacenents' which had been accumulating over a number of years and said that 'the scope for encouraging, through fiscal and other measures, the practice of ploughing back of profits for replacements or other capital expenditure, should be examined as early as possible.' The Taxation Enquiry Commission also said that although the situation had improved in recent years, there was still a good deal of leeway to be made up by industrial enterprise in India.

The above view has been contested by many business men. According to them, industry was not able to carry out replacements, because there was difficulty in getting the capital goods from foreign countries and not because it was unwilling to plough back profits into the undertaking. According to a survey carried out by the Employers' Association, Calcutta, the total assets of 138 selected companies increased, during the period 1946-50, from Rs 335.3 crores to Rs 422.8 crores (an increase of Rs 87.5 crores) and, of this, Rs 26.5 crores were in respect of depreciation provisions and Rs 16.7 crores due to the ploughing back of profits. Actually, expenditure on block capital was even more: as much as Rs 47.0 crores were spent on this item. On the assumption that the sample survey represented 20 per cent of the whole private sector, according to this Association, the expenditure incurred on block capital during the above four-year period was in the neighbourhood of Rs 235 crores—not an inconsiderable figure

when viewed against the fact that the total paid-up capital of the sector in 1946-47 was about Rs 400 crores.[1] It was, therefore, argued that, if there was a leeway still to be made up, the same should be done by Government. 'In the interest of maintaining progress and improving general efficiency, industry should be asked to bear only half the net differential cost, while Government should agree to grant additional depreciation allowances, on a tax-free basis, for the remainder.'

All this is based on the argument that industrial profits have not been adequate. Now, whether profits are adequate or not is largely a matter of opinion. Industry naturally argues that, unless profits are on a given scale, capital and enterprise would not be attracted to business: others (i.e. the Government and the public) may hold a contrary view and say that, while there may be scope for certain further facilities being granted by Government, the scale of profits is unduly high—especially in the context of a 'socialistic pattern of society'.

Data in regard to trends in company profits and their allocations are, however, rather inadequate in this country. Until 1951, the index of profits was compiled by the Office of the Economic Adviser, Ministry of Commerce and Industry, Government of India, and thereafter it is collected by the Reserve Bank of India. According to the figures compiled by Government (with 1950 base=100), even net profits have been well over 115 since 1954. It cannot, therefore, be argued that profits are 'inadequate'.[2]

The next question is how the profits which have accrued are being allocated. Here also, the information available is inadequate. Information in some detail with regard to the allocation of profits is available in the Report of the Taxation Enquiry Commission for a sample of 496 public companies for the period 1946-51 and in a survey made by the Reserve Bank of India for a sample of 746 public companies for 1950-52.[3] These two samples comprise companies having a paid-up capital of Rs 5 lakhs and above, and cover 19 major

[1] *Depreciation Allowances and Replacement Costs,* issued by the Employers' Association, Calcutta, December 1952.

[2] Vide Appendices IX and X.

[3] Vide *Company Finances in India, 1950-52,* published in the Reserve Bank of India Bulletin, July 1955.

industrial groups. According to the Taxation Enquiry Commission's analysis, during the period 1946-51, tax provision, distributed profits, and retained profits, as percentages of profit before tax, constituted 44 per cent, 32 per cent and 23 per cent respectively. During 1950-51, the percentages were 41 per cent, 37 per cent and 22 per cent respectively. The corresponding figures in the U.S.A. during 1949 were 40 per cent, 28 per cent and 32 per cent.[1]

Of late, the Reserve Bank of India has been making regular studies of the trend of company profits. According to these, profits after taxation were quite high till 1955, compared to what they were in 1951-54. With 1950 base=100, profits after taxation stood at 149.8 in 1955, but fell down to 114.4 in 1958. Profits before taxation were higher, the index number being 150.8 in 1955 and 168.7 in 1958.[2]

These indices, however, measure the trends in the absolute quantum of profits. To assess the profitability of companies, one has to refer to the ratios of profits to capital employed or to net worth. Two index series for measuring this latter trend have also been prepared by the Reserve Bank.[3] These show that there has been a steady fall since 1955. The fall need not, however, cause undue alarm or worry. It has to be borne in mind that a part of the capital employed or net worth brought in through additional capital resources (e.g. loans from the World Bank to the iron and steel industry) would take time to be fully effective. During the period of gestation, the return on capital employed is bound to be static or even low.

Further studies carried out by the Reserve Bank of India in 1961 shew that, during 1959, there was a remarkable increase in profits, but a substantial portion of the same was ploughed back. Other notable features of the operating results were substantial increases in sales and other income on the income side, and salaries and wages, and excise duty on the expenditure side.[4]

The set-back since 1955 cannot be ascribed to any fall in

[1] Quoted in *Depreciation Allowances and Replacement Costs* issued by the Employers' Association, Calcutta.

[2] Vide Appendices IX and X.

[3] Vide Appendix XI.

[4] *Reserve Bank of India Bulletin*, September 1961.

the turnover of the companies which, as a matter of fact, continued to rise. The set-back appears to have been caused more by larger provisions for depreciation and taxation than any other factor. Another contributing factor has been the increase in the volume of Union excise duties, which increased from Rs 52.55 crores in 1955 to Rs 159.06 crores in 1959. In the Reserve Bank studies, profits before tax have been arrived at after deduction of excise duty payments: as the latter have gone up sharply in recent years, profits before tax have naturally fallen.

A study made by the Research Division of the Indian Institute of Public Opinion, New Delhi, reveals the following facts for the period 1950-58:

	1950	1955	1958
Profits before tax as percentage of income	6.31	7.37	5.76
Net fixed assets as percentage of income	28.42	32.90	40.91
Profits before tax as percentage of net fixed assets	22.21	22.40	14.08

These figures show that additional investment is taking place steadily, even though profits may be falling.

On the other hand, the movement of profits in particular industries has been very different from the average for all industries taken together. In industries like tobacco, cotton textiles, vegetable oils, cement, coal, jute and tea, for example, profits are falling rather steadily, and it is this fact which gives rise to the cry that Government's fiscal policy is acting as a brake on further industrial development.

The latest figures reveal two notable trends, viz. (*a*) that the growth in fixed assets and inventories was much smaller than in previous years and (*b*) that the sales and profits recorded only a moderate rise in spite of the inflationary conditions prevailing in the economy. While the amount spent on 'raw materials and other manufacturing expenses' showed only a moderate increase from Rs 1,015.54 crores in 1958 to Rs 1,081.41 crores in 1959, there was a much greater rise in payment towards excise duty and expenditure on meeting 'other expenses' comprising salaries and wages, employers' contributions to welfare schemes, interest etc.

Thus, the excise duty paid rose from Rs 149.16 crores to Rs 159.06 crores, or by 6.6 per cent and 'other expenses' from Rs 493.21 crores to Rs 542.47 crores, or by 9.9 per cent, at the end of 1959 over the previous year 1958. While gross expenses thus recorded a rise, the sales expanded from Rs 1,831.66 crores in 1958 to Rs 2,002.15 crores in 1959—an increase of 8.1 per cent. Profits after tax also increased—from Rs 64.97 crores in 1958 to Rs 102.37 crores in 1959.[1]

Trend in Dividends

A point often made is that the fall in the rate of dividends in recent years is acting as a disincentive to further investment. Now, during the period 1951-58, most of the company managements followed a liberal policy with regard to the allocation of profits to dividends. Of the total profits available for distribution and for ploughing back in business, on an average, 60% were distributed to the shareholders during the period 1951-55 and over 64% during the years 1956-58. As percentage of equity share capital, the dividend rate has ranged between 8.2 and 11.8 per cent.[2] We thus see that, although the days of spectacular dividends are over, it cannot be argued that dividends paid to shareholders have been drastically slashed down.

Future of Profits and Private Enterprise

A good deal of outcry has lately been heard about the future of profits in the private sector. While production has been steadily on the increase, it has been argued by some that this tempo cannot be maintained indefinitely, because (*a*) productivity (as opposed to production) is not rising and (*b*) the future of profits is dark. Now, neither of these two statements stands the test of scrutiny. In so far as productivity is concerned, contrary to popular belief, it has risen appreciably over the past few years. It is often overlooked that average productivity does not depend on the performance of labour alone: it is a function of the combined input of a number of other factors which are almost as important,

[1] *Reserve Bank of India Bulletin*, September 1961.
[2] Vide Appendix XII.

e.g. equipment, resources, organisation and management. According to a note prepared by the Labour Bureau, while the index of gross ouput per worker at constant prices (with 1953=100) was 86.6 in 1947, it stood at 132.7 in 1958—the latest year for which figures are available. The ECAFE report for 1959 also shows that, although productivity is low compared with countries in Europe, the output per worker has been rising steadily in recent years. The moral, in so far as industrial enterprise is concerned, therefore, is that the factor of productivity should not act as a damper.

As regards the future of profits, we have seen already that, contrary to popular belief, these have not been going down at all. Despite the heavy taxation of both personal incomes and company profits, most well-managed companies have been declaring good dividends. If the prices of scrips on the Stock Exchanges are any guide, entrepreneurs in India today are having a very good time indeed. In the protected economy which has been brought into existence through the compulsion of rapid development, almost unlimited opportunities have been thrown open to private enterprise.

Profits apart, both entrepreneurs and managements still manage to secure for themselves various kinds of "fringe benefits"—of which the ordinary shareholder is hardly aware. Some of them manage to have incomes which remain high despite taxes and regulations. Others have "expense accounts" of a far-reaching character. As noted earlier, even the stringent provisions of the amended Indian Companies Act have not been able to put a stop to undesirable, but not illegal, company practices which enable business men to earn commissions and incomes to which, strictly speaking, they are not entitled. Finally, entrepreneurs and managers do not always think in terms of the money they earn: more than money, they value the prestige and power that go with the direction and management of industry.[1] Therefore, even if profits were to remain stationary for a few years, these other benefits and advantages would continue to provide the necessary incentives to our entrepreneurs and managers.

[1] For a brilliant exposition of the incentives of prestige and power, the reader is referred to C. Wright Mills, *The Power Elite*, New York, 1957, and Vance Packard, *Status Seekers*, New York, 1960.

CHAPTER XIII

INDUSTRIAL ENTERPRISE AND THE PUBLIC SECTOR

The Evolution of the Public Sector

THE STORY OF THE EVOLUTION of the public sector in the economy and polity of India is a very recent one. Unlike in Western countries like the U.K., France, Germany, Sweden and Italy, its history in India can be compressed within the last decade, or, to be more precise, within the period following the attainment of independence by India in 1947.[1]

Although planning has been the main topic in India ever since the Congress Party assumed power in the Provinces in 1937, the idea that development should be promoted by the State actually managing industrial concerns did not take root until well after 1947.[2] As we have seen already, it was only after a Constitution had been framed laying down the 'Directive Principles' of State policy that the matter assumed importance. The issue received its final imprimatur or seal of approval in the Report of the Planning Commission dated 7 December 1952. There was a definite acceptance of the principle of nationalisation, together with the general caveat that even those undertakings which would operate in the private sector might have to be subjected to State regulation and guidance.

The specific projects and enterprises which have been initiated in the public sector since 1947, may be classified under five broad heads: (*a*) defence and strategic establishments; (*b*) public utility undertakings; (*c*) shipping; (*d*) industries proper; (*e*) other projects.[3]

[1] Prior to 1947, there was virtually no 'public sector' in the Indian economy. The only instances worthy of mention were (*a*) the Railways, (*b*) the Posts & Telegraphs Dept., (*c*) the Port Trusts, (*d*) the Reserve Bank of India, (*e*) the Ordnance and Aircraft factories and (*f*) a few State-managed undertakings like the Government salt factories, quinine factories etc.

[2] Even the Report of the National Planning Committee, set up under the auspices of the Indian National Congress, did not envisage the setting up of large industries to be owned by the State. It spoke more of control and regulation of economic activities by the State in the national interest rather than of the latter actually taking part in such activities.

[3] For details, see N. Das, *The Public Sector in India*, Bombay, 1961.

We are concerned here with industries and other projects only. Of these, the most important are the Sindri Fertilisers and Chemicals, Ltd., the Hindustan Machine Tools, Ltd., the National Instruments, Ltd., the Hindustan Housing Factory, Ltd., the Indian Rare Earths, Ltd., the Hindustan Antibiotics, Ltd., the Bharat Electronics Ltd., the Hindustan Cables, Ltd., the Chittaranjan Locomotive Works, the Integral Coach Factory, the Indian Refineries, Ltd., and the three steel plants set up at Rourkeila, Bhilai and Durgapur respectively. In addition to these, which have been sponsored by the Central Government, there are projects sponsored by the Governments of the constituent States: the most important of these are the U.P. Government Cement Factory, the Superphosphate Factory of the Bihar Government, the Sirsilk, Ltd., (producing artificial silk) in Hyderabad, the Sirpur Paper Mills and the Coke Oven *cum* Gas Grid Project in Durgapur, West Bengal.

An idea of the relative importance of the public and private sectors in the country today may be gauged from the fact that at the end of 1950-51, the book value of gross fixed assets owned by the Central and State Governments, together with the working capital in the enterprises concerned, amounted to Rs 1,236 crores, as compared to Rs 875 crores at the end of 1947-48.[1] Of the former, Railways alone (including Railway industries like the Chittaranjan Locomotive Works) accounted for Rs 837 crores; and industries proper, Rs 44 crores.

In the First Five-Year Plan, the total investment in the economy was Rs 3,360 crores, out of which investment in the public sector was Rs 1,560 crores. In the Second Plan, which commenced on 1 April 1956, and ended on 31 March 1961, the target of investment in the two sectors combined was Rs 6,750 crores, the ratio of public to private investment being 54:46. During the Third Five-Year Plan period, the investment envisaged in the public sector alone is Rs 6,300 crores, while that in the private sector would be about Rs 4,100 crores.[2]

[1] As against this, the value of the productive assets in the private sector (excluding agriculture, small-scale industry, transport and residential housing) in 1950 was estimated at Rs 1,472 crores. Vide *The First Five-Year Plan*, New Delhi, 1952.

[2] Planning Commission, *The Third Five-Year Plan*, New Delhi, 1961.

The above figures represent investment (or expenditure) in all spheres of economic and social activity. Even in the restricted sphere of large-scale industries, minerals and electric power, however, the accent on investment in the public sector has increased progressively since 1951, when the First Plan was launched. The ratio of the projected expenditure under these heads in the public and private sectors in the Third Plan is over 2:1 as against less than 1:1 in the First Plan.

Problems Posed by the Public Sector

The assumption of direct responsibility for industrial development by the State raises problems of various kinds—both internal and external. The internal problems are those relating to (*a*) organisation, (*b*) price-fixing and (*c*) labour relations. As regards external problems, the very fact that a considerable proportion of the capital and enterprise of the country flows into the public sector has its impact on the flow of capital and enterprise into the private sector.

Let us consider the internal problems first. The most important of the internal problems is that of organisation, i.e. how the socialised industries should be managed so as to yield the highest production at the least cost. While no uniform rule can be laid down regarding the form of organisation in a nationalised undertaking, the general pattern in almost all countries is that such undertakings are managed by quasi-independent corporations. The success or failure of such a corporation depends largely on the quality of the Board directing it, as it is the Board which takes most decisions on policy and all decisions on administration. Unlike that of a private company, the Board of a State undertaking has a special responsibility to the consumers, the employees, the Government and indeed to the entire nation. The composition of the Board and the manner in which the members thereof are selected are, therefore, very important from more than one point of view. While there cannot be any rigid rule about the size of such a Board, it is obvious that selection should be confined to persons who have wide experience in the appropriate field of activity.

What should be the powers and responsibilities of such a

Board? In a private undertaking, the Board of Directors is responsible only to the shareholders, but the very concept of a State undertaking implies a certain degree of control of policy by Government. At the same time, efficiency can be secured only by decentralisation of management. The question is how to strike a balance between these two conflicting principles. This, however, is an exceedingly delicate and difficult task. Excessive use of parliamentary control may diminish the autonomy of the Board and undermine its ability to make quick decisions and secure efficient management.[1]

The other two internal problems are those of price-fixing and labour relations. As regards the former, intricate social and other considerations complicate the issue. While private industry must, in the long run, receive prices which cover total costs (including taxes) and provide sufficient net return to attract venture capital, Government may allow extra-commercial considerations to enter into the determination of its supply prices. 'The interests of Government are inevitably broader than those of private enterprise. The consequence to cost calculation of broader public interst is that almost every Government-produced good is more than one good—it is a good providing individual utility to the buyer, while at the same time providing utility to the community in terms of more general welfare. Hence the operation of some public industries at less than cost (the remainder to be made up from the general revenues) can be justified.'[2] There is, however, a danger that in those public undertakings which partake of the character of 'insulated' monopolies, prices may be fixed not at less than cost, but even at well above cost. In a private enterprise, competition provides the 'natural safeguard' for the consumer: although the primary aim is to maximise profits, the service rendered to the consumer is also an incidental consequence and the forces of competition help to bring the prices to the level of actual costs. In a public undertaking, on the other hand, the 'take it or leave it' attitude is likely to dominate and make it extremely difficult for the consumer to influence price policy.

[1] Ernest Davies, *National Enterprise*, London, 1956. See also N. Das, *The Public Sector in India*, Bombay, 1961, Chapter VII.

[2] Philip E. Taylor, *The Economics of Public Finance*, New York, 1956.

Labour relations also take on a special character in a State-managed undertaking. With the advantage of being able to work under insulated and often non-competitive conditions, labour wants to make its influence felt in two ways—(*a*) by demanding representation on the executive boards or on bodies associated with such boards and (*b*) by securing special benefits (e.g. higher wages, security of service, better housing and other amenities) for itself. The former demand impinges on the managerial organisation while the latter affects prices. And this has its repercussions on the private sector as well. It is not possible to isolate the workers in the public sector from those in private undertakings: so when the former demand a 'correct' or 'scientific' wage, the question arises whether such a wage can be granted without causing repercussions on costs and also on the general wage level in the country as a whole.[1]

The Organisational Set-up in India

In India, the joint-stock form of organisation has been attempted in most of the industrial undertakings in the public sector. The capital of these joint-stock companies is fully contributed by Government and is held in the name of the President (or the Governor) except that a few shares are held in the name of one or two officials, because the establishment of a private limited company requires at least two shareholders.[2] In form, these companies are like any other companies: they have an elaborate memorandum and articles of association; these latter provide for share transfers, general meetings and all the other paraphernalia of a joint-stock company. But in actual practice this is all on paper, because generally a single Government (sometimes two Governments) is the shareholder. The Boards of Directors of these companies are all nominated by the controlling Government and they follow a general pattern. There is a Chairman, who is generally the Secretary of the Ministry in charge of the particular

[1] United Nations, *Some Problems in the Organisation and Administration of Public Enterprise in the Industrial Field*, New York, 1954.

[2] Nearly two-thirds of the Government companies have been organised as 'private limited' companies. The word 'private' has, however, been dropped, as it gave the anomalous impression that the companies concerned were not Government undertakings.

enterprise. There is invariably one officer, generally from the Finance Ministry, of the rank of Joint Secretary. There are officials of one or two other Ministries who have close connection with the working of the particular enterprise. All these Directors are nominated *ex officio* and, therefore, any transfer in their postings means a change in the composition of the Board of Directors. In most of these Boards, there is also a sprinkling of a few non-officials—one or two business men and sometimes a labour leader.

As regards concerns which are not fully, but only partly, owned by Government, the Government reserves the right to nominate a certain proportion of the Directors. Their number varies with the proportion of the Government's shareholding and the relationship of Government with that particular concern. A large number of the Directors nominated by Government are officials who are connected with the particular activity and the rest are non-officials who are considered to be experienced in that particular line. In most of these concerns, Government reserves certain special rights: for example, Government's approval has to be obtained for the raising of new capital, for large expenditure on certain items and for the appointment of top officers..

The organisational set-up of industrial undertakings in the public sector has evoked a good deal of criticism in recent months. Although the joint-stock form of organisation is now the rule rather than the exception,[1] in actual practice the advantages of elasticity and efficient management have not been fully secured. 'The lack of definite rules laying down their relationship with the controlling Government, the legislature, the labour employed, the consumer and the general public, has meant in many cases lack of proper accountability which has led to its being described as a "fraud on the constitution".'[2]

In the new Companies Act, Government companies have been assigned a special position. A Government company is

[1] At a certain stage, Government held the view that a statutory semi-autonomous corporation was better than a joint-stock company, but this view no longer finds acceptance.

[2] *The Indian Economic Journal*, Bombay, October 1954.

defined as one in which the Central and State Governments alone or together hold at least 51 per cent of the share capital. In such cases, Government has the power to determine which provisions of the Act should appply.[1] This provision has been criticised in many quarters on two principal grounds: (*a*) the provision is discriminatory against companies in the private sector and (*b*) it takes out Government companies from the general orbit of State control and regulation. Even if all or most of the shares are held by Government, there is no justification for discriminatory provisions. It cannot be argued that, either at the bureaucratic or political levels, the amount of incompetence and corruption is less than is common among the less well-managed companies in the private sector. Where an enterprise is run entirely as a departmental responsibility, there is the usual control of Parliament; where it is not so and Government chooses to adopt the company method, there is no reason why it should not subject itself to its disabilities as well, when it seeks the privileges of the corporate structure.'[2]

The same view was expressed by a number of members of Parliament at the time the Companies Bill was debated on the floor of the House. 'These provisions would enable Government to exempt so-called Government companies from the control of both the Parliament and the Act.' 'All real power is taken in the hands of the executive and would be liable to the vagaries of executive discretion without any real control by Parliament.'

On behalf of Government, it was argued that Government companies, owing to the very fact that they represent public interest and not the interests of groups of shareholders, should stand on a different footing from companies in the private sector. It was pointed out, for example, that the provisions requiring the supply of information to shareholders and the submission of returns, as also the power given to the Auditor General to direct the manner in which audit should take place, to conduct suplementary and test audits, and to

[1] The power is given by Section 620 of the Act. In actual practice, however, this power is exercisable by Government subject to the overall control of Parliament. It is also significant that, to date, no occasion has arisen requiring Government to make use of this power.

[2] *The Eastern Economist*, New Delhi, 29 July 1955.

comment on the audit report (the comments of the Auditor General are required to be placed before the general body meeting) provided adequate safeguards against executive tyranny.

It is very difficult to say at this stage whether this conferring of a special status to Government companies, as defined in the Act, would ultimately be in the national interest. In this matter, a compromise has been attempted between two conflicting considerations. On the one hand, it has been felt that State undertakings, which have as their objective the promotion of something above and beyond the interests of private shareholders must have a certain amount of freedom which cannot be accorded to enterprises operating within the private sector. Control of State undertakings should, therefore, be exercised through a different set of rules and practices and the State must be the ultimate authority to decide what these rules and practices should be. On the other hand, there is no case for autonomous Statutory Corporations, as such institutions tend to operate as independent bodies with objectives and policies often at variance with the general economic policy of the Government of the day. In the new Act, a golden mean has been attempted between autonomy and control.

The problem of management of State industries has also been discussed in the recent reports of the Estimates Committee of the Parliament. On many occasions, the Committee has pronounced a categorical disapproval of industries run on a departmental basis—which it considers unsuitable for any public or commercial activity except for Posts and Telegraphs and, to some extent, the Railways. The Committee has remarked that the setting up of undertakings as public limited companies has not also improved matters. 'For all practical purposes, they have functioned like private limited companies and, in spite of the safeguards which Parliament recently provided in giving a special position to Government companies under the new company law, it is unlikely that this would change matters.' This, however, runs counter to the other point made by the Committee, viz. that the Directors of the Boards of various public undertakings, being mostly nominated officials of Government with no experience

of business management, have not contributed to the efficient functioning of industry. The Committee has, therefore, recommended the abolition of the present system of nomination and its substitution by a Board of Managing Directors consisting of men of wide experience, preferably from private business or those who have some knowledge of financial and technical matters. 'This Board must be given the freedom to which they have been accustomed in their own particular fields of activity and a new system of relationship should be found between the Minister and the Board which would terminate the existing departmental status of public undertakings.'[1]

Difficulties have arisen mainly from the 'dilemma of public enterprise', viz. the effort to achieve both business flexibility and public accountability. The dilemma has occurred because of the insistence on *maximum* flexibility as well as *maximum* accountability. Unfortunately, the greater the insistence on accountability, the less the possibility of being flexible, and vice versa. One cannot have the best of both worlds.[2]

The question of price-fixing has also posed difficult problems for undertakings in the public sector in our country. The latest thesis that State enterprises should be so conducted as to yield 'planned profits', was first enunciated at the All-India Congress Committee Seminar on Planning at Ooty in June 1959. Now, this overlooks two important facts. Firstly, in a private enterprise economy, competition, however imperfect, provides a natural safeguard for the consumer. In a public undertaking, on the other hand, the 'take it or leave it' attitude makes it extremely easy for Government to inflate the price of the product. Secondly, a 'profit-price policy' provides a convenient cover for inefficiency. In a private enterprise, competition ensures a reasonable standard of efficient operation, but in India, where many public-sector undertakings do not yet satisfy the normal commercial tests for efficiency, prices may be, and are, artificially boosted so

[1] *Thirty-third Report of the Estimates Committee of Parliament, 1958-59*, New Delhi, 1959.

[2] For a detailed exposition of this 'dilemma', the reader is referred to the author's *The Public Sector in India*, Bombay, 1961, Chapter VII. See also A. H. Hanson, *Public Enterprise and Economic Development*, London, 1959.

as to yield a profit, thereby shifting the cost of inefficiency to consumers.

As regards industrial relations in State undertakings, all that need be said here is that the mere fact that Government is the employer has not ushered in a new era of industrial harmony. Industrial disputes and strikes have taken place, and will continue to take place, in these undertakings as well, simply because, in a democratic society, trade unions are largely conditioned in their outlook and practices by the capitalism which produced them. Secondly, almost all workers' organisations in India are associated, either directly or indirectly, with political parties. As long as this association continues, it would be difficult to conduct industrial relations even in public undertakings from a purely economic angle.

The fact which is often lost sight of is that ownership and management of undertakings by the State is not an end in itself, but a means to an end. The goal is the securing of maximum benefits for all sections of the community. Nationalisation by itself may mean no more than the fact that the proprietary interest vests in the State and that the profit-making motive has been abolished. But, if the social implications of public ownership and operation are to be realised, there should be full recognition of the community's right to the most ample service or supplies at the lowest possible price. Socialisation implies the full acceptance, both by the management and employers, of the principle of a social objective, viz. that of serving the public good. All this would require a much greater degree of fairness, objectivity and mutual respect on the part of all the three parties, viz. the management, the employees and the consumers, than has been displayed so far.

A Factual Note on Government Companies

On the 31 March 1961, there were 139 Government companies at work in the country and their paid-up capital totalled Rs 498.4 crores, as against only 61 companies with a total paid-up capital of Rs 66.0 crores in 1955-56. Although the number of these Government companies is still much less than that of non-Government companies, the paid-up

capital is quite high, as will be evident from the following Table:

Position of Government Companies in the Total Corporate Sector

Year ending	Govt. Cos.		Non-Govt. Cos.	
	No.	Paid-up Capital	No.	Paid-up Capital
		(In crores of Rupees)		
1955-56	61	66.0	29,813	958.2
1956-57	74	72.6	29,283	1,005.0
1957-58	91	256.8	28,189	1,049.5
1958-59	103	424.2	27,376	1,085.6
1959-60	125	468.4	26,796	1,124.7
1960-61	139	498.4	25,969	1,226.2

A study recently carried out by the Reserve Bank of India in respect of 50 representative Government companies shows that while the total paid-up capital was Rs 463.73 crores, borrowings amounted to Rs. 287.6 crores (including Rs. 266.01 crores from Government alone). The gross fixed assets amounted to Rs 544.1 crores, total depreciation Rs. 50.84 crores, inventories Rs 82.79 crores, and other assets Rs 29.32 crores.[1]

[1] *Reserve Bank of India Bulletin*, January, 1962.

Chapter XIV

SAVINGS, INVESTMENT AND CAPITAL FORMATION

India's Potential Financial Resources

We have seen in an earlier chapter that, until recently, the flow of enterprise into industrial undertakings was governed, to a considerable extent, by the availability of finance. Although the situation has altered considerably during the past two decades or so, finance, in the sense of the ultimate financial resources of the country, has not ceased to be important. The emphasis has, however, shifted from its quantitative aspect to the aspect of its mobility and quality, from the 'mechanics' of finance to its 'physics'.

Even a rough estimate of the 'total financial resources' available in the country is difficult because it includes such indeterminate items as (*a*) the resources of moneylenders and indigenous bankers and (*b*) the hoards. We know more or less accurately the total paid-up capital, reserves and deposits of agencies like the joint-stock banks, exchange banks, co-operative banks, insurance companies and post-office savings banks, but we have no exact information about the quantum of capital handled by the indigenous shroffs. It is true that in their evidence before the Committee on Finance for the Private Sector, the Bombay Shroffs' Association stated that the annual turnover of their members was about Rs 100 crores, but they could not furnish any figures regarding the amount of finance lent by them to small and medium-scale industries to meet their requirements of working capital.

As regards hoards, we are equally in the dark. Many conflicting statements have been made in the past regarding the amount of hoards in existence, but this has been due largely to the fact that the word *hoarding* was used rather loosely. It was argued that it is the locking up of surpluses in gold or silver bullion or coin, which hampers economic development, and not the industrial and social use of the precious metals. Even if we concede this, it cannot be denied that a considerable amount of money is being 'hoarded' as

gold bullion or coin. The only difference in the situation as it obtains to-day and as it was, say, fifty years ago, is that, in those days, it was the cultivators and landowners who used to lock up their surplus earnings in silver or gold. The slow but steady erosion of their incomes, caused by such factors as increased cost of living, higher taxation and the taking over of large landholdings by Government, has compelled this class of people to disgorge most of their hoards. Their place has, however, been taken by a new class of hoarders, viz. profiteers, blackmarketeers and traders. Two factors have been responsible for the recent spurt in hoarding. Firstly, the high taxes on personal income and wealth, which have been a feature of the Indian taxation system since 1946, have prompted many people to conceal their income in the form of gold bullion. Secondly, the almost continuously inflationary situation which has been prevalent since World War II has shaken the confidence of a certain section of the moneyed people in the stability of the rupee: they are clinging to bullion as the only 'safe' investment—safer than even industrial securities.

Whatever the reasons for hoarding, the locking up of investible funds in bullion retards economic development. At a time when Government is in need of increasing funds to meet its obligations under the Five Year Plans, its anxiety to get at these hoards is understandable. Unfortunately, no practical method has been devised whereby this idle money can be put to economic use. Government is using the language of both gentle persuasion and threat, but the hoarders are well aware of the difficulties of officialdom. As long as Government is unable to put a stop to the large-scale evasion of taxes on personal income and wealth and also to curb the inflationary spiral, hoarding (with its attendant evil, the smuggling of gold and silver) will continue unabated.

Factors Inhibiting Investment in the Private Sector

What are the reasons which tend to inhibit investment in the private sector? Now, private investment is governed by two principal factors, viz. willingness and ability to invest. The willingness to invest may be reduced by economic, political or psychological uncertainties. Then again, the ability to

invest may be diminished by contraction of the savings available to the private sector. Both these factors have been at work in India.

It was stated by the Committee on Finance for the private Sector that willingness to invest was affected by (*a*) the threat of nationalisation, (*b*) procedural uncertainties and difficulties, (*c*) Government's labour policy and labour legislation and (*d*) various forms of control and regulation.[1] Let us consider these factors one by one.

Firstly, we may consider the threat of nationalisation. 'There is, in the country, a widespread feeling that, despite the importance given to private investment in the Five-Year Plans, private enterprise is in practice tolerated rather than accepted as an instrument of development.' This feeling has been reinforced by the series of legislative measures undertaken in recent years to regulate the private sector and also by the amendment of the Constitution making the fairness of compensation, in the event of nationalisation, a non-justiciable issue. Frequent references to the statutory power of nationalisation by Government spokesmen have in the past increased rather than allayed the fears of potential investors and entrepreneurs.

The second inhibiting factor consists in the procedural uncertainties and difficulties in starting a new enterprise or expanding an existing enterprise. These have been caused directly by the regulative powers assumed by the State. Firstly, any party wishing to establish a new unit or substantially to expand an existing unit in a 'scheduled' industry must take out a licence under the Industries (Development and Regulation) Act. This usually takes at least three to six months from the date of application. Secondly, if financing such a project involved floatation of new issues on the capital market, sanction for the issue must also be obtained from the Controller of Capital Issues. And if the project requires the importation of machinery or other material, import licences and foreign exchange must be secured. All these steps have to be taken by any promoter of a new unit, in addition to compliance with the normal procedure laid down in the Indian Companies Act. 'While these regulations have

[1] *Report of the Committee on Finance for the Private Sector*, Bombay, 1954, Ch. III.

the legitimate purpose of conserving domestic and foreign capital and canalising them into desired channels of activity, they have also the effect of delaying and retarding private investment.' The inevitable bureaucratic delay in dealing with applications has also been an important inhibiting factor.[1]

The third cause which is said to have had a considerable adverse repercussion on private investment is Government's labour policy and labour legislation. With the increase in the cost of living in the war and post-war years, a variety of additional obligations to compensate labour have been imposed by legislative measures adopted by the Central and State Governments and by the Awards of Industrial Tribunals. Apart from the effect of these measures on the costs of labour to industry, they have greatly reduced the freedom of employers to adjust the labour complement or to enforce disciplinary measures or to rationalise in order to step up productivity. Ultimately, they have adversely affected initiative and the flow of venture capital, with deleterious consequences on expansion and modernisation.

Finally, there are some industries which are subject to special regulations in regard to price, production or distribution. In the coal, cement and iron and steel industries, for example, prices are fixed and distribution of the product regulated by Government. Price or distribution controls or both are also operative in respect of the products of a number of other industries, under the Supply and Prices of Goods Act, 1950. These are said to have hindered the maximum mobilisation of internal resources for the expansion or rehabilitation of industry. 'In the case of steel and electricity undertakings in particular, the restrictions imposed by Government have not only limited the internal resources of these industries, but rendered difficult the attraction of new capital, because of the low rate of return on investment.'

As regards diminution of the *ability* to invest, the following facts are relevant. Such factors as increased labour costs and restrictions on prices have not only affected the *willingness* to invest but have also reduced the quantum of resources that could be utilised for reinvestment. Secondly, the price rises in the war and post-war years, along with increased

[1] Government has recently taken certain steps to speed up the disposal of applications.

taxation, have reduced the capacity of fixed income earners to save. Again, as a result of the social and political changes which have occurred in the past few years, some of the traditional investing classes like the princes and the zamindars have ceased to be substantial supporters of the investment market.

The heavy borrowings by Government also have had their repercussions on private investment in the industrial sector. Since 1951-52, borrowings by Governments in the organised capital market have been substantial.[1] There has been a considerable diversion of voluntary savings into Government Securities and correspondingly the resources available for investment in industrial shares and debentures have been reduced. In the past, the reduced confidence in industrial management as a result of malpractices by some sections of the entrepreneurial community also contributed to this preference for Government Securities. 'There were several weaknesses within the private sector itself which tended to make the investors shy of subscribing to industrial shares and debentures.'

The investment climate has, however, changed considerably since the inception of the Second Five-Year Plan. In so far as personal savings are concerned, it appears that more and more people are becoming investment-conscious. The number of shareholders who have put in their savings in shares and debentures of industrial undertakings has gone up appreciably. As a matter of fact, the striking success of several industrial issues of established companies, or even of new companies when they have been promoted by entrepreneurs in whom the public have confidence, is a proof of the broadening character of the investment market in India. In many such cases, the number of applications received and shares applied for were far in excess of the shares offered.[2] Of late, some of the new issues have been offered at a premium and yet they have been snapped up in no time.

At the same time, it is doubtful if the *ordinary* man has really become investment-conscious. The upward shift in the prices of agricultural products and the large outlay by Govern-

[1] Vide Appendix XXIII.
[2] For details, see H. T. Parekh, *The Future of Joint-Stock Enterprise in India*, Bombay, 1958.

ment in the rural areas have added to the income of the agriculturists and, to some extent, some of these latter have been investing a part of their additional earnings in certain types of undertakings. But the factory workers and the so-called middle classes do not appear to have changed their investment habits. Although the real earnings of factory workers have increased, they are still inclined to spend their extra income on immediate consumption. As regards the middle classes, their real earnings have actually gone down and hence, even if they had the *wish* to save, they do not have the *capacity* to do so. Most of the new investors are drawn from the ranks of members of the *upper* middle class and of such business men and traders as have made a lot of money since the days of World War II.

A recent study conducted by the Reserve Bank of India also supports the above view.[1] Although the authors of this study have sought to establish that 'there has taken place in recent years some broadening of investment by people in shares', the statistics quoted by them show that, between 1955-56 and 1958-59 (the latest year for which figures are available), (*a*) the largest increase in the number of share-holders took place in the income-group *above* Rs. 25,000 (the percentage increase was 36.7 as against an increase of 23.7 per cent in the income-group below Rs 25,000), and (*b*) the proportion of shareholders in the income-range *below* Rs 5,000 actually declined from 52.2 per cent in 1955-56 to 48.2 per cent in 1958-59 while that above Rs 5,000 increased from 47.8 per cent to 51.8 per cent. In other words, *share-holders in the upper income-range continue to be the main prop of the investment market in India.* The figures cited by the Reserve Bank of India conclusively prove that, while the investment market has broadened to some extent, it has not broadened in such a manner as to make India's capitalist sector a 'people's capitalism'.

Scope for Mobilisation of Untapped Resources

There are many people who believe that the sources of capital have not dried up, but that instead they have merely shifted from the urban to the rural sector. According to this school

[1] Vide the article entitled '*Broadening of Investment in Shares in India*', published in the Reserve Bank of India Bulletin for December, 1960.

of thought, what is needed is intensive propaganda among the new class of 'potential' investors and the creation of 'facilities' for the mobilisation of such savings.[1] There has been tremendous increase in agricultural production in rural areas, and cottage and village industries have also received a new fillip as a result of the more positive policies pursued by the State. According to the Planning Commission, the largest addition to national output was to have come from the agricultural sector and, in due course, agriculture and cottage and hand industries (mostly distributed in rural areas and small towns) were expected to make as much contribution to the national output as all the other sectors put together. The expectations have largely materialised. In their latest Report, published in 1961, the Central Statistical Organisation estimated that, of the total net national product of India in 1960-61 amounting to Rs 12,690 crores, at 1948-49 prices, as much as Rs 5,860 crores or nearly 46 per cent was contributed by agriculture, animal husbandry and allied activities. The corresponding figures in 1949-50 were Rs. 8,820 crores and Rs 4,360 crores respectively.[2]

In other words, the national income has been increasing in the rural areas also, both absolutely and relatively. It is true that part of the increase is being used up in consumption, but as was pointed out in the *General Report on All-India Rural Credit Survey*, a good slice of the increased purchasing power in the rural areas could be mobilised into productive channels if proper investment facilities were provided in those areas. The private credit agencies (i.e. the commercial banks and indigenous bankers and moneylenders) operating in these areas were not able to tap these increased earnings in any satisfactory measure.

In recent years, various steps have been taken by Government to mobilise such savings. The integrated scheme of rural credit drawn up by the Committee of Direction of the Reserve Bank of India has not only facilitated agricultural and other rural operations, but also made more funds available for investment in other sectors. The setting up of the State Bank

[1] This view was expressed by the Committee of Direction of the Reserve Bank of India in their *General Report on All-India Credit Survey*, Bombay, 1954.

[2] Vide Appendix XXXII.

of India, with the avowed objective of bringing banking facilities within the reach of the remotest village or small town, has also facilitated the mobilisation of untapped savings. Finally, the Small Savings movement (giving various incentives to different classes of potential savers) has also helped.

The above viewpoint was stressed in the survey on the 'Mobilisation of Domestic Capital in certain countries of Asia and the Far East' issued by the ECAFE as early as 1951. Starting with the thesis that agriculture must provide a substantial part of the domestic resources necessary for economic development, the ECAFE report said that until the peasant could be assured of access to working finance on reasonable terms, he was not likely to be able to make any substantial contribution to the growth of development capital. 'There do exist pockets of sizeable surpluses of income over expenditure. Potential savings are waiting to be garnered and it is up to the Government to offer the necessary inducements and facilities to smoothen the process of mobilisation.'[1]

Since 1955, the State Bank of India has been pursuing a policy of progressive branch expansion in accordance with its statutory obligation to open not less than 400 branches in five years. By the end of December 1961, 416 such branches had been opened. The other commercial banks (scheduled and non-scheduled) had also opened some 423 branches during the period 1955 to 1959.

As a result of all this activity, the aggregate deposits of commercial banks have been increasing progressively. From Rs. 1,043.8 crores in 1955, these went up to the record level of Rs. 1,854.6 crores in 1960. Although a sizeable part of the increase in deposits represents the counterpart fund of P.L. 480 imports, the net rise in deposits was significant. As stressed by the Reserve Bank of India in their Annual Report on the Trend and Progress of Banking in India in 1960, this was indicative of the gradual spread of the banking habit among the people and the effort of the banking system in mobilising savings. This was substantiated by two facts: firstly, over the period 1955-59, both the number of 'personal' savings and fixed deposit accounts as well as the outstanding balances in them showed a relatively larger

[1] ECAFE, *Mobilisation of Domestic Capital in Certain Countries of Asia and the Far East*, Bangkok, 1951.

rise than those of 'business' and 'other accounts'. Secondly, the rate of deposit expansion was generally higher in centres with population of 50,000 and less, than in the other centres.[1]

The General Problem of Savings, Investment and Capital Formation

The fact is that the *per capita* real national income of the people is increasing, as will be evident from the following table:

Estimates of Per Capita Real National Income[2]

Year	*Per capita income* (Rs at 1948/49 prices)	*Index* (1948-49 = 100)
1950-51	247.3	102.3
1951-52	250.3	105.2
1952-53	255.7	109.4
1953-54	266.7	116.0
1954-55	267.8	118.8
1955-56	267.8	121.2
1956-57	275.6	127.2
1957-58	276.4	125.9
1958-59	280.2	134.7
1959-60	289.0	137.0
1960-61	292.5	146.7

These figures should, however, be taken with a certain degree of reserve. It is conceivable that while the *per capita* income is going up, the income of large sectors of the population might be stationary or might even be going down.[3]

The question is whether the increase in *per capita* real national income is finding its way into productive channels, i.e. whether it is being converted into savings which can be utilised for development. An interesting analysis has recently been made by the Reserve Bank of India which throws some light on the trend of savings in various sectors during the period 1950-51 to 1958-59.[4] According to this study, aggregate savings steadily increased from 1951-52 till 1956-57 (with the exception of 1953-54, when it declined slightly),

[1] Reserve Bank of India, *Trend and Progress of Banking in India during the year 1959*, Bombay, 1960.

[2] Central Statistical Organisation, New Delhi: *Monthly Abstract of Statistics.*

[3] Vide the inaugural address of Mr. H. V. R. Iengar, Governor of the Reserve Bank of India, at the Second Indian Conference on Research on National Income, held at New Delhi on 31 August 1960, quoted in the author's article entitled '*The Economic Position of the Average Indian Today*' in the Golden Jubilee Number (1961) of *Commerce*, Bombay.

[4] Vide article entitled '*Estimates of Savings and Investment in the Indian Economy*' published in the *Reserve Bank of India Bulletin*, August, 1961. Vide also Appendix XXIV.

but declined in 1957-58 and made only a partial recovery in 1958-59.[1] It is significant that (*a*) the average savings during the period 1951-52 to 1958-59 were only 5.8 per cent of the average national income and (*b*) the aggregate marginal saving-income ratio declined from 19.1 per cent in 1953-56 to 17.3 per cent in 1956-59.

Analysing the figures separately, sector by sector, one notices wide fluctuations from year to year. During the past four years, however, there has been appreciable increase in the savings of the rural household sector, but those in the urban household sector have remained more or less constant. Now, savings in the household sector comprise (*a*) liquid assets like currency, bank deposits and gold, (*b*) financial assets like shares, securities and insurance policies, and (*c*) physical assets like house, property, agricultural implements, etc., held by individuals/families.

It is interesting to note that savings in the household sector were the largest in the form of physical assets, gold, currency and Government securities, the average share of these items in the total being about 81.3 per cent. This shows that the average person still prefers to invest his savings in these rather than in buying insurance policies or industrial shares/debentures. It is true that "small savings" increased from Rs. 38.5 crores in 1951-52 to Rs. 100 crores in 1960-61, but such savings do not represent investment in industry.

What is the position in regard to capital formation? Total investment in the economy amounted to Rs. 3,360 crores during the First Plan period, of which public investment accounted for Rs. 1,560 crores and private investment Rs. 1,800 crores. The corresponding figures during the Second Plan period were Rs. 3,650 crores in the public sector and Rs. 3,150 crores in the private sector. Thus, total investment in the Second Plan was about double that in the First Plan and private investment in the Second Plan was about 72 per cent higher than in the First Plan. The investments proposed in the Third Plan are even higher—in both the sectors. These do not, however, represent net savings made by the community. A considerable portion of these investments is, and would be, accounted for by foreign aid and deficit financing.

In any case, we are concerned more with private investment in organised industries. Of course, this has been increasing steadily, the annual average during the Second Plan period having been Rs. 140 crores as against the annual average of Rs. 46.46 crores during the previous quinquennium. The gross fixed assets of all non-financial non-Government companies also increased from Rs. 119.75 crores in 1951-52 to Rs. 263.35 crores in 1957-58, while the figures of consents for capital issues showed a similar rise—from Rs. 45.33 crores in 1951 to Rs. 125.06 crores in 1959. But, as has been emphasised by the National Council of Applied Economic Research, "while it is possible to show that the level of investment in the economy has risen in recent years, there are no indications that the rate of domestic savings has correspondingly increased."[1]

Indian Taxation Policy and Private Investment

A good deal of controversy has raged in recent years over the effects of taxation policy on private investment. Businessmen and entrepreneurs have been complaining that the taxation policy of Government sucks them dry and leaves little room for initiative, enterprise and investment. 'Statistics' have been put forward to show that 'capital' is disappearing from the private sector and that the policy of 'dividend slash' is having a distinctly harmful effect on future investment.[2] We have seen, however, that *actual* investment in the private sector has not diminished, but rather increased, both in quantity and quality, during all these years.

There are one or two important points which should be borne in mind in this connexion. All Governments nowadays require an increasing volume of public revenue and, more so, when the avowed objective is the establishment of a Welfare State. No doubt, there is a limit to taxable capacity and

[1] National Council of Applied Economic Research, *Taxation and Private Investment*, New Delhi, 1961. According to the Council, over the Second Plan period, the *rate* of savings in the economy had not risen at all, but had stagnated around 8 per cent of the national income.

[2] Vide arguments adduced in two pamphlets, '*Where is Capital gone?*' and '*Whither leads a Dividend Slash?*', issued by the Employers' Association, Calcutta, 1949.

the limiting factor is generally taken to be the estimated wealth of a country. Ordinarily, this is taken to be the overall national product, but this limit refers only to a point of time. The capacity to pay (i.e. taxable capacity) is never constant—on the contrary it is ever changing, except when the employable resources have been fully exploited and the economy has reached a full employment level. 'In a developing economy, the capacity is not inflexible. The limits to taxation in such an economy are more psychological than physical. The quality of public administration, the degree of public consciousness and the extent of confidence in the Government's expenditure policy on the part of those who are called upon to pay the taxes are the deciding factors in this psychological limit.' In other words, as long as the tax proceeds are properly utilised for developmental purposes, adding progressively to the size of the national income, there can be no real limit to taxation. 'If there are visible symptoms of taxable capacity being exhausted in such an economy, it will be the result of a *psychological* crisis and not of a real *physical* crisis in the economy.' In India, too, taxable capacity should be viewed from this broad and dynamic angle and not from the static, physical angle.

Even so, there is an upper safe limit to taxation. According to Colin Clark, the safe limit is 25 per cent of the national production.[1] Although this precise figure has been contested by a number of economists,[2] we may accept this as a working formula for the purpose of examining the present and foreseeable burden of taxation in our country. In India, this upper limit has not been reached yet and is not likely to be reached even under the scheme of development proposed in the Third Five-Year Plan. As a matter of fact, if the trend of events is any guide, business men are working just as hard under high tax-rates as they would have done under low tax-rates.

Moreover, tax is paid ultimately by individuals and not by

[1] Colin Clark has proved this 'limit' by making close studies of the price-index, tax-level and its relation to the national income in a number of countries.

[2] E.g. Benjamin Higgins, Joseph A. Pechman and Thomas Mayor. Colin Clark's analysis has been attempted with a purpose: with statistics, any conclusion can be shown to be valid.

groups. Even in the same income-bracket, the capacity of any two individuals to bear the tax load is not identical. Taxes evoke reactions individually and sometimes the most vociferous are those who are the best organised, but not necessarily the hardest hit.

In its recent report on the economic effects of the present tax system on private savings and investment, the National Council of Applied Economic Research has made some interesting observations. For instance, it has said that the combined impact of income and wealth taxes has curtailed the ability to save *only at the very high income levels*. While the rate of aggregate savings has not kept pace with the rate of investment, the overall climate for private investment has remained favourable and the desire to invest in equity shares continues to be as keen as ever.[1]

The Need for Genuine Investment Trusts

As hinted already, the future investment outlook is not at all gloomy. The lot of the private investor in India, however, is by no means easy or pleasant. In the eyes of the Government, he is simply a part of the private sector intent on getting returns out of all proportion to his investment. He also has to contend with the fact that, on Indian stock exchanges, it is the speculator rather than the genuine investor who calls the tune. In such a situation, the stock market, instead of being a barometer of the economic outlook, becomes a distorting mirror and, to the other difficulties of the investor, is added that of judging and allowing for the extent of distortion caused by the quite irrational behaviour of speculators caught up in the excitement of the bull market. Not unnaturally, the genuine investor feels baffled and perplexed.

If investment is to proceed along healthy lines, the investor must be able to judge when the market value of his scrip has gone beyond the point that would be justified by a reasonable assessment of growth prospects. This, however, is not easy for the ordinary man seeking to put in his savings in industrial shares. The responsibility can be undertaken only

[1] National Council of Applied Economic Research, *Taxation and Private Investment*, New Delhi, 1961.

by Unit Trusts, Investment Clubs and other devices which have proved so successful in the U.K. and the U.S.A. We have very few genuine Investment Trusts in our country today. If Unit Trusts could be set up on the Western model, the investor would have at his disposal the expert knowledge of persons who know the *real* market conditions. He would then come forward with greater confidence and alacrity.

There would be a further indirect gain in so far as the objective of a socialist pattern of society is concerned. By helping the widest possible diffusion of ownership of shares, such Investment Trusts would provide a most effective method to counter concentration of economic power. 'A people's capitalism or shareholders' democracy may well turn out to be the real socialist pattern of society.'

Development Savings Bank Scheme

Various techniques have been suggested from time to time to mobilise internal resources, but no serious efforts appear to have been made to tap the wages-and-salaries sector of the economy. It would be useful, therefore, to make a brief reference here to a Development Savings Bank Scheme formulated by Mr. C. Loganathan of Ceylon. This has been approved by the banking and fiscal authorities in many countries in the world and now forms the central pillar of Ceylon's Ten-Year Plan. The Scheme is based primarily on (*a*) voluntary and compulsory contributions from wages and salaries to be credited to the accounts of the salary- and wage-earners themselves in their individual names in a Development Savings Bank and (*b*) contributions by employers to the accounts of the employees as a percentage of salaries and/or net profits. It visualises tax rebates to taxpayers for the above types of contributions, so that the incentive of a person to earn is not stifled and, at the same time, he is compelled or induced to use a part of his wealth in promoting economic development. Under the Scheme, employees in the different enterprises can also be permitted to transfer their provident-fund balances in their accounts to the Development Savings Bank for investment, if they so desire. The investment can take the form of shares in Unit Trusts embracing many

enterprises so that the risk would be fairly well spread.[1]

The scheme has been recently approved in principle by the International Chamber of Commerce. It is undoubtedly an attractive scheme, but the crucial question is whether, in the present political climate, such a measure of compulsory contributions can be enforced in our country. Perhaps the Planning Commission could hold tripartite discussions and see to what extent employers' and workers' organisations are prepared to support such a scheme.

[1] For further details, see *The Eastern Economist*, New Delhi, 9 December 1960.

CHAPTER XV

THE FUTURE OF INDUSTRIAL ENTERPRISE IN INDIA

The Gloomy Prophets

EVER SINCE Government announced its policy of fostering a 'mixed economy' (i.e. the co-existence of public and private sectors) in the country, all kinds of doubts and misgivings were expressed, not merely by business men and industrialists, but by responsible economists and 'neutral' members of the public. Measures adopted to 'control, regulate and direct' industry were criticised—sometimes in violent terms—and the fear was expressed that Government's policy would lead the country to the verge of bankruptcy. In particular, it was asserted that the assumption of greater and still greater responsibilities by the State would be too much for the administration to bear and whispers were gleefully exchanged that one day Government would be compelled, by the sheer logic of events and circumstances, to retrace its steps. But, today, at the beginning of the Third Five-Year Plan period, Government's plans and policies stand largely vindicated. Not only has there been no fall in production, but there have been appreciable rises—both in the agricultural and industrial sectors. Even in terms of productivity per wage-earner or man-hour, there has been a distinct improvement, though one might wish that it could have been better still. As regards the flow of investment and enterprise into the private sector, notwithstanding the so-called irritating and irksome restrictions flowing directly from the economic and fiscal policies pursued by Government, there has been no diminution in activity. If the price-movements of the share-scrips of industrial concerns are any guide, one might almost say that private enterprise never had it so good.

An Objective Analysis of Pitfalls and Dangers

The fact that India has made progress should not, however, make us feel complacent. 'India continues to make progress, but she should be making, and has the capacity to make,

far greater progress than she has done so far.'[1] There are no obstacles in the sector of financial resources: the obstacles, if any, are in the sector of 'incentives'. A Government does not need incentives: it is driven as much by the spur of the people's displeasure as by the personal ambition or sense of public service of individual members. But the private sector would still need 'incentives'. Would the necessary 'incentives' be there in the years ahead?

We have seen already that, despite the heavy taxation of both personal incomes and business profits, entrepreneurs and managements still manage to retain for themselves a good slice of the 'fruits' of industry. The prestige and power that go with direction and management of industry also inspire them to work harder and better. For the next few years at least, these incentives are likely to continue undiminished.

It would be foolish, however, for entrepreneurs in the private sector not to take note of the overall policy of the State. More than once it has been emphasised by Government that (*a*) the old motive of making huge profits must be replaced by a new motive of serving the country and its people, with only limited profits, (*b*) workers should be treated as partners in industry and not as mere producers of goods, and (*c*) there should be awareness of a social purpose in even the most private undertaking. In their own interest, business men must gradually adjust themselves to this new concept of the rôle of private enterprise in our country.

This adjustment will naturally take some time. As, however, economic development is being furthered in this country through a democratic process and not as an imposition from the top (it is a unique experiment and has probably no parallel in any other country of the world), there are reasons for cherishing the hope that the adjustment will ultimately take place. Echoes of this adjustment are to be found in the statements made by many leading industrialists that they have taken note of the new ideology and are quite willing to fall in line with Government's policy. As one industrialist said: 'Bold planning and determined execution of large schemes of

[1] *The Eastern Economist*, New Delhi, Special Budget Number, 1959-60, March 1960.

development are essential if we are to raise living standards, relieve unemployment, give opportunities to all and ensure a reasonable degree of social justice. We welcome a situation in which both State Enterprise and Free Enterprise can, side by side, play their important rôles. We should not close our eyes to the enormous changes that have occurred in the capitalist countries throughout the world. Modern capitalism has changed beyond recognition from what it was a century ago. It has shown a remarkable capacity to fit into the most modern concepts of the Welfare State.' Some cynics have, however, attributed this revised stand of India's industrial leaders to 'enlightened self-interest'; others have argued that the 'leopard does not change his spots' and hinted that these pious statements mask a deep conspiracy to sabotage Government's programme of ushering in a socialist pattern of society. While it is not denied that even today some employers have not been able to adjust themselves to the new situation, it would not be fair to say that the business community as a whole consists of 'hypocrites, sycophants and moral cowards'.

Today, the business community has to do its job in the face of tremendous odds. Apart from the Governmental restrictions and regulations to which they have to submit, they also have to face a tax burden which, by all international standards, is one of the highest in the world.[1] Further irritants are frequently added in the shape of public statements by Ministers and others, denouncing either particular industrial groups for their alleged acts of omission and commission, or the entire private sector. For instance, during the year 1960 alone, wild statements have been made by responsible persons (who should have known better) that (*a*) the private sector is far too dependent on financial assistance from Government (this allegation was disproved with the help of facts and figures by the President of the Federation of Indian Chambers

[1] Even the World Bank Mission, in a Report published early in 1960, expressed its grave concern about the multiplicity of controls which have proved highly vexatious to private enterprise in India. The Mission also commented on the currently widespread belief in Government circles that profits were immoral and spoke disapprovingly of certain measures to regulate profits by taxation and price control. 'Arbitrary methods in deciding what the limits to profit should be, are liable to discourage investments and handicap the financing of further expansion.' Vide *The Eastern Economist*, New Delhi, 15 July 1960.

of Commerce & Industry), (*b*) it is the employers who stand in the way of modernisation and rationalisation of cotton mills (that this was not so was conclusively established by the Indian Cotton Mills' Federation in a very able memorandum), (*c*) free enterprise inevitably leads to monopoly (this was ably refuted by a number of leading financial and commercial journals of Bombay and Calcutta), and (*d*) private entrepreneurs are anxious to see that the Five-Year Plans of Government do not succeed (this was such a malicious and sweeping statement that even those who had no love lost for the private sector were dumbfounded). As we have seen already, private interprise has more than fulfilled its share of the Plans. If it has not been able to do better, the responsibility lies at least in part with Government, which has sometimes subjected the private sector to avoidable harassment.[1]

Too much reliance is sometimes placed on the superior ability of the public sector to 'deliver the goods'. It is argued that, if rapid development is to be achieved, it must be done consciously, i.e. through the apparatus of the State (or the public sector) and should not be left to the free interplay of so-called economic laws only. Although, theoretically, this may appear quite logical, the practical limitations of the State apparatus (limitations of human resources, of the administrative machinery and even of investible resources) would make it extremely difficult for Government to carry the entire burden of industrial development. The recent failure on the part of the public sector to provide adequate power and transport for the requirements of industry furnishes a typical example of the unwisdom of attempting too much on all fronts.

The dangers of bureaucratic red-tape and formalism should not also be overlooked. On the one hand, various controls and regulations have vested enormous powers in the hands of Government officials, and the private sector as well as the general public are often put to needless harassment, inconvenience and delay by the 'little bureaucrats'. The arguments put forward by Mr. N. C. Chatterji in his dissenting minute

[1] This view has been expressed by many independent foreign observers, journalists and economists. Attention is invited in this connection to the *Quarterly Economic Reports* issued by the Indian Institute of Public Opinion, New Delhi.

on the Report of the Select Committee on the Companies Bill are well worth quoting in this context: 'It is one thing to prescribe restrictions, limitations or fetters sitting in a Select Committee or discussing a Bill in the placid atmosphere of a legislative chamber. Yet the sum total may create an impracticable situation from the point of view of company formation or the practical working of a business concern. It is not wise to drive the private sector to the tender mercies of a bureaucracy, as this may lead to jobbery and corruption.'

There is the possibility of bureaucratic red tape and formalism exhibiting themselves in the management of industrial undertakings in the public sector as well. Although strenuous efforts have been, and are being, made to entrust the management of such undertakings to the same type of Board as obtains in the private sector, with adequate scope for initiative and enterprise, old practices and prejudices die hard. It is to be hoped that authority will have the imagination and boldness to permit the unfettered use of discretion within a fairly large orbit of operation.

Finally, there is the pitfall inherent in the lack of adequate entrepreneurial ability within the ambit of Government officialdom. Recruited to discharge an entirely different type of responsibility, unacquainted with the needs of business and industry, unfamiliar with practices and procedures which have resulted in a high level of efficiency and productivity in the private sector, Government officials, barring a few notable exceptions, are sometimes unequal to the new tasks and responsibilities which have been assigned to them. It is true that some of them are learning the technique of business administration through trial and error, but this is a costly method of acquiring experience and, in the process, incalculable harm may be caused to programmes and plans of development. It may be uncharitable to hold one company's misdemeanour as proof enough to indict all managements in the public sector, but the public sector ought not to expect, as a matter of right, that the maximum allowance should be made for its shortcomings or that it should be judged by its good intentions rather than by its good performance.[1]

It should not also be forgotten that, in modern industrial

[1] Vide the author's *The Public Sector in India*, Bombay, 1961.

undertakings, the scope of functions of the management has expanded both in volume and in complexity. 'While the volume of work increases in arithmetical progression, the complexity of functions and their relationships increase in geometrical progression.'[1] The task of a successful organisation is to co-ordinate the different factors of production in such a way that the maximum possible output is secured at the least possible cost, without undermining the required quality standard of the product. This is as true of the public as of the private sector.

The Third Five-Year Plan

It would be appropriate at this stage to consider the programme envisaged in the Third Five-Year Plan period, as this must inevitably affect private industrial enterprise for the next five years. The objectives in view are more or less the same as in the Second Plan, viz. (*a*) to attain a rapid growth of the national economy by increasing the scope and importance of the public sector and in this way to advance to a socialist pattern of society, (*b*) to develop basic heavy industries for the manufacture of producer goods, (*c*) to secure a large expansion of employment opportunities, and (*d*) to achieve a reduction of inequalities in income and wealth and a more even distribution of economic power.[2] In concrete terms, the Plan envisages an investment of Rs 10,400 crores so that the national income can increase by at least 5 per cent per annum.

The size of the Plan has received the general blessing of the Indian business community, but the respective allocation of investment between the public and private sectors has invited some criticism. It has been suggested that the State is proposing to take upon itself a responsibility which it may find difficult to discharge—particularly in the light of the national and human resources likely to be available. Far too optimistic estimates have been made of (*a*) the resources that can be raised within the country and (*b*) the assistance that

[1] R. C. Davis, *Industrial Organisation and Management*, New York, 1950.
[2] The Third Five-Year Plan stresses that 'the benefits of economic development should accrue more to the relatively less privileged classes of society, and there should be a progressive reduction in the concentration of income, wealth and economic power'.

may be expected to be received from abroad. Secondly, while the mistakes of the two preceding Plans in respect of planning and organisation have been admitted (reference has been made, for instance, to the lack of speed, economy and integrity within the administrative set-up), the cures which have been suggested do not go to the root of the matter and are mere palliatives.

A glaring weakness of the Plan is its confused thinking over the question of prices. According to the Third Plan, inflation during the Second Plan period has been of the order of 30 per cent only. Actually, it is much more : the figure of 30 per cent has been arrived at on the basis of wholesale prices, but, as is well known, retail prices have moved up at a much steeper rate. Yet, the Plan merely says that, with the progressive step-up in investment, an upward pressure on prices is inevitable. It has completely overlooked the fact that the rise in prices has adversely affected the cost of living of the population at most levels, and further inflationary pressure which would result from the gigantic investment programme of the Third Plan must cause additional sufferings to the common man. It is not denied that some rise in the price level is inevitable in a developing economy, but the Planning Commission has made no concrete suggestions to arrest a deterioration in the situation.[1]

Nevertheless, from the standpoint of private enterprise in the country, the programmes included in the Third Plan are welcome in the sense that they would give further stimulus to industrial development on all fronts. If the price line can be held, if the necessary resources can be mobilised and if the administrative machinery can be streamlined (these are all big 'ifs'), private enterprise would benefit, despite the fact that its proportionate share in the total allocation is less than what it was in the two earlier Plans.

The Private Sector will Continue to Function

It would, therefore, be a mistake to conclude that industrial enterprise in the private sector is on its 'last legs'. We have

[1] The most disappointing feature of the section on Price Policy in the Third Five-Year Plan is that it merely repeats old platitudes. Vide the author's *Spotlight on Indian Economic Problems*, Calcutta, 1961.

already referred to the mental readjustment which is being made by the business community in the background of the new values which have been enunciated and the new policies which have been laid down. Part of this readjustment may have been compulsive, but it would not be fair to dub the *entire* business community 'a horde of exploiters, always trying to outwit Government and get round all restrictive laws and regulations'. A few black sheep often tarnish the reputation of a whole group. Undoubtedly, there are persons who continue to think on the old lines, viz. that, with their astuteness and command of wealth, they can manage to evade many of the rules and regulations of Government. But such persons are definitely on the decrease. At the worst, the business community in India, as in most democratic countries in the West, is guided simply by 'enlightened self-interest'.[1]

There are three important facts inherent in the economic situation, which afford cogent reasons for cherishing the hope that business enterprise in the private sector will continue to flourish. The first is that consumer demand has been considerably stimulated by the impact of heavy developmental expenditure undertaken by the State. This demand will increase still further as more money is injected into the economic system. Secondly, every outlay in the public sector directly generates demand for goods and services in the private sector. When the State decides to set up a steel plant of a fertiliser factory in the public sector, it is not in a position to undertake by itself all the operations connected with the setting up of the plant or factory. It has to fall back upon persons or firms in the private sector for the supply of relevant goods and services. Thirdly, the very products of public undertakings stimulate the setting up of other enterprises and these have inevitably to be in the private sector. Thus, supplies of fabricated steel, billets and sheets give rise to industries which can use these materials for the manufacture of various items of household and other industrial use: the production of lathes helps the

[1] The 'round-up of business opinions', conducted by the *Indian Institute of Public Opinion*, New Delhi, from time to time, also tells the same story. It is true that the bulletins and memoranda issued by various Chambers of Commerce, Trades Associations and Employers' Organisations sometimes present a different picture, but these latter are meant to emphasise a 'particular point of view', and points of view have to be couched in rather strong language if they are to make an impression.

setting up of engineering units; the production of heavy machines assists a number of industries engaged in the manufacture of consumer goods. Such instances could be multiplied *ad infinitum*. Enough has been said, however, to show that these three factors have given, and will continue to give, the private sector a new 'dynamism'. This will become even more pronounced as the Third Five-Year Plan comes into operation.[1]

The main reason for saying that private industrial enterprise has still a large and important part to play in this country is that India's approach towards the socialist pattern of society is not doctrinaire, but pragmatic. Notwithstanding the occasional outbursts of certain political leaders, including the Prime Minister of India, the present Government does not want socialism for its own sake. The accent is on a Welfare State and a reduction in inequalities of income and wealth, and not on expropriation of private profits, be it land or business. In other words, if private industrial enterprise can attune itself to the new outlook, the need for expropriation or nationalisation of *existing* undertakings may never arise. Not only that: it may find that it has an honourable place in society and is not being just tolerated.

Duties of the Private Sector

Private enterprise must, however, think in terms of the interests of the consumers and the common people and not in terms of shareholders only[2]. Secondly, it must make genuine efforts to diffuse economic power. In the present context of Government's policy (and most of the people are solidly behind Government on this particular issue), concentration of power in a few hands or groups is bound to invite countervailing State action. It would be extremely foolish of private enterprise, therefore, to take a short-term view of the situation and 'make hay while the sun shines', for the sun may not shine for long.

[1] N. Das, *The Public Sector in India*, Bombay, 1961.

[2] The Third Five-Year Plan says as follows: 'The socialist pattern of society envisaged in India's Plans does not imply that all economic initiative must rest with the State. Indeed, it assigns to private enterprise an important role in national development. The private sector must, however, accept the broad discipline and values implied in the national Plan and must function in unison with the public sector.'

The private sector has a part to play in this matter of diffusion of control. Firstly, it should endeavour to secure a very wide dispersal of the ownership of equity capital. At present, the ups and downs in the profitability of industries are a matter of concern to a class of shareholders who are numerically insufficient in relation to the total population.[1] When not only wealthy capitalists, but lower middle class salary-earners, industial workers and peasants become shareholders, the masses will have a bigger stake in the stability and progress of private industry. The word 'capitalist' would then cease to be a term of opprobrium: a broad-based public opinion would then demand that Government refrain from policies which tend to undermine the profitability of industry. Secondly, managements must abide by a more enlightened code of conduct—a code which would place them above reproach in so far as the public are concerned. They must strive assiduously not to create a situation which might compel the State to assume strong countervailing powers. In other words, the countervailing powers should come from within the managements themselves. Freedom and democracy in the economic field can be rightfully demanded by private enterprise only when it is imbued with a social purpose and does not seek power for a limited few.

[1] According to the Department of Company Law Administration, New Delhi, in 1957-58, the number of companies that had less than 50 shareholders each was 2,600 out of a total of 8,379.

APPENDICES

APPENDIX I

JOINT-STOCK COMPANIES REGISTERED AND AT WORK

Year ended 31st March	Number	Paid-up Capital (in crores of rupees)	Average Paid-up Capital per company (in lakhs of rupees)
1948	22,675	569.6	2.51
1949	25,340	628.3	2.48
1950	27,558	723.9	2.63
1951	28,532	775.4	2.72
1952	29,223	855.8	2.93
1953	29,312	897.6	3.06
1954	29,492	941.2	3.19
1955	29,625	969.6	3.27
1956	29,874	1,024.2	3.42
1957	29,357	1,077.6	3.67
1958	28,280	1,306.3	4.61
1959	27,403	1,515.6	5.53
1960	26,921	1,593.1	5.91
1961*	26,108	1,724.6	6.60

* Figures provisional.
Source : *Annual Reports on the Working of Joint-Stock Companies in India.*

APPENDIX II

YEAR-WISE ACCOUNT OF COMPANIES NEWLY REGISTERED AND LIQUIDATED

(In crores of rupees)

Year		New Registrations		Liquidations	
		No.	Authorised Capital (Rs)	No.	Paid-up Capital (Rs)
1947-48	..	3,267	283.9	628	9.0
1950-51	..	2,104	120.7	830	9.1
1951-52	..	1,866	152.2	1,244	9.2
1952-53	..	1,333	96.4	1,244	11.3
1953-54	..	1,193	155.3	933	8.8
1954-55	..	1,203	225.9	938	9.1
1955-56	..	1,448	156.9	1,021	12.7
1956-57	..	848	210.6	1,135	13.0
1957-58	..	961	102.7	2,001	12.7
1958-59	..	1,095	284.3	1,979	15.8
1959-60	..	1,452	160.5	1,870	7.9
1960-61	..	1,683	286.7	2,401	12.33

Source: *Monthly Blue Book of Joint-Stock Companies in India.*

APPENDIX III
COMPANY FAILURES IN INDIA
(In crores of rupees)

Averages		New Registrations		Liquidations	
		No.	Paid-up Capital	No.	Paid-up Capital
1915-19	..	199	0.5	189	1.3
1920-24	..	726	1.8	285	6.4
1925-29	..	553	0.7	335	6.6
1930-34	..	891	0.9	382	6.7
1935-39	..	1,054	1.2	634	5.5
1940-44	..	1,182	1.4	648	3.6
1948-55	..	2,082	6.6	975	9.0
1955-61	..	1,248	6.1	1,746	12.5

Source: *Monthly Blue Book of Joint-Stock Companies in India.*

APPENDIX IV
REMUNERATION OF MANAGING AGENTS DURING 1946-51 & 1955-59

Industry		Average of Remuneration Per Annum				Remuneration as percentage of Profits*	
		No. of companies	1946-51 (in lakhs of Rs)	No. of companies	1955-59 (in lakhs of Rs)	1946-51	1955-59
Cotton Textiles	..	96	3,18	204	2,88	16.4	16.0
Jute Textiles	..	47	1,50	44	63	20.3	18.9
Other Textiles	..	12	6	11	27	13.8	9.9
Iron & Steel	..	3	48	2	50	7.3	3.3
Engineering	..	52	32	82	1,14	12.0	11.5
Sugar	..	22	28	73	85	15.8	11.3
Chemicals	..	29	10	43	25	14.8	13.7
Paper	..	7	18	13	45	11.2	11.2
Vegetable oil	..	7	5	15	7	13.1	12.4
Matches	..	4	18	4	10	15.4	12.0
Cement	..	8	29	11	60	0.3	10.6
Plantation: (*a*) Tea	..	76	33	167	57	12.0	11.6
(*b*) Others	..	11	2	43	9	13.0	9.4
Coal	..	17	29	47	37	16.7	14.4
Electricity	..	22	30	21	42	18.1	10.2
Shipping	..	11	27	10	30	21.4	12.3
Others	..	55	31	211	1,14	5.5	10.1
TOTAL	..	479	814	1,001	10,67	13.7	11.1

* 'Profits' means profits before tax (excluding depreciations and interest charges) and includes managing agency remuneration.

Source: 1. For information for 1946-51: *Report of the Taxation Enquiry Commission*, 1955.
2. For 1955-59 data: *Reserve Bank of India Bulletin.*

APPENDIX V

DISTRIBUTION OF NEW COMPANIES ACCORDING TO THE FORM OF THEIR MANAGEMENT

Form of Management	1956-57	1957-58	1958-59	1959-60	1960-61
Managing Agents ..	14	15	7	14	21
Managers ..	2	1	1	3	3
Secretaries and Treasurers	1	1	7	3	1
Managing Directors ..	197	227	250	508	596
Directors ..	634	717	830	924	1,062
TOTAL	848	961	1,095	1,452	1,683

Source: *Department of Company Law Administration, New Delhi.*

APPENDIX VI

SHARE AND DEBENTURE CAPITAL ISSUED BY THE MAJOR INDUSTRIES IN INDIA

(In lakhs of rupees)

Industry and Year	No. of Companies	Paid-up Share Capital				Debenture Capital		Total of Paid-up Capital & Debenture Capital (Rs)
		Ordinary (Rs)	Percentage to total	Preference (Rs)	% to total	Amount (Rs)	% to total	
Cotton Textiles								
1955	63	3,619.2	85.9	546.2	12.9	48.7	1.2	4,214.1
1959	60	3,918.1	76.8	900.5	17.7	285.5	5.5	5,104.1
Jute Textiles								
1955	60	2,131.0	67.8	712.8	22.7	229.8	9.5	3,143.6
1959	27	1,892.7	66.9	750.2	26.4	188.2	6.7	2,831.1
Tea								
1955	128	773.2	90.0	83.3	9.7	2.5	0.3	859.0
1959	106	937.3	92.3	75.3	7.9	2.5	0.2	1,015.1
Sugar								
1955	26	479.3	77.2	130.5	21.0	11.0	1.3	620.8
1959	24	541.7	79.2	108.0	15.8	34.5	5.0	684.2
Coal								
1955	51	818.0	77.2	124.8	11.8	117.0	11.0	1,059.8
1959	43	731.7	85.9	111.8	13.2	7.8	0.9	851.3
Engineering								
1955	N.A.	N.A.	—	N.A.	—	N.A.	—	N.A.
1959	28	5,552.0	72.5	1,585.6	20.7	520.0	6.8	7,657.6

Note: Position for 1955 is as on 31st March, and for 1959 as on 31st December.

Source: *The Investor's India Year Book*, 1955 and 1960. (Place, Siddons and Gough, Calcutta)

APPENDIX VII
PRIVATE COMPANIES REGISTERED IN INDIA AND AT WORK
(Capital in crores of rupees)

Year	All companies		Private Companies		Precentage of private companies to all companies	
	No.	Paid-up Capital (Rs)	No.	Paid-up Capital (Rs)	No.	Paid-up Capital (Rs)
1927-28	5,830	276.4	1,722	71.5	29.5	25.5
1933-34	9,434	300.8	3,698	98.7	39.2	32.8
1938-39	11,114	290.0	5,255	77.0	47.3	26.6
1945-46	17,343	424.0	7,214	101.0	42.2	24.1
1950-51	28,532	775.4	15,964	208.9	55.9	26.9
1951-52	29,223	855.8	16,810	248.9	57.5	29.0
1952-53	29,312	897.6	17,257	268.8	57.5	29.9
1953-54	29,528	944.9	19,280	313.6	65.3	33.2
1954-55	29,779	983.1	19,720	327.1	66.5	33.3
1955-56	29,874	1,024.1	20,299	333.8	67.9	32.5
1956-57	29,357	1,077.6	20,547	363.0	69.9	33.6
1957-58	28,280	1,306.3	19,984	532.7	70.6	40.7
1958-59	27,403	1,515.6	19,757	710.6	72.9	46.8
1959-60	26,921	1,593.1	19,615	781.5	72.8	49.0
1960-61	26,108	1,724.6	19,363	848.5	74.1	49.1

Source: 1. *Progress of Joint-Stock Companies in India.*
2. *Monthly Blue Book of Joint-Stock Companies.*

APPENDIX VIII
INDEX OF INDUSTRIAL PROFITS—ALL INDUSTRIES
(Base: 1950—100)

Year	Gross Profits including Depreciation	Profits		Profits after tax as percentage of net worth *
		Before Tax	After Tax	
1950	100.0	100.0	100.0	100.0
1951	128.7	132.4	131.6	124.7
1952	99.0	86.6	78.8	74.0
1953	109.6	100.9	98.1	88.3
1954	125.1	121.6	115.2	101.3
1955	150.8	150.1	149.8	122.1
1956	165.0	167.2	158.3	118.1
1957	151.7	133.7	116.4	84.1
1958	168.7	151.7	114.4	96.4

* 'Net Worth' means paid-up capital plus all reserves (other than taxation and depreciation reserves) and balance of profit.

Source: *Reserve Bank of India Bulletin.*

APPENDIX IX

INDEX OF GROSS INDUSTRIAL PROFITS INCLUDING DEPRECIATION

(Base 1950 = 100)

Industry	1951	1953	1955	1957	1958
I. *Plantation Industry* ..	63.0	121.6	89.4	64.7	82.0
1. Tea	64.1	140.8	82.5	71.6	89.4
2. Coffee	132.9	121.7	171.8	171.5	167.3
II. *Mining & Quarrying* ..	119.7	152.5	169.9	210.7	215.8
3. Coal	108.2	94.9	132.4	141.1	151.4
III. *Processing & Manufacture—Foodstuffs, Textiles & Products thereof*	140.9	100.4	140.3	105.8	124.3
4. Vegetable Oils ..	71.6	141.9	189.3	92.9	220.2
5. Cotton Textiles ..	145.4	90.8	145.2	71.7	81.5
6. Jute Textiles	145.5	72.5	62.7	84.4	131.9
IV. *Processing & Manufacture—Metals, Chemicals, Minerals, etc.*	123.4	119.2	217.2	250.7	276.8
7. Iron & Steel	132.8	141.8	234.3	214.8	242.7
8. Engineering (*a*) ..	117.3	115.9	255.2	335.7	353.9
9. Chemicals (*b*) ..	113.4	105.8	151.9	212.7	235.5
10. Matches	99.7	104.8	95.5	89.0	110.4
V. *Processing & Manufacture—Not elsewhere classified* ..	151.6	127.6	181.6	206.9	233.6
11. Cement	128.0	124.5	168.9	160.5	177.0
VI. *Other Industries*	122.7	86.4	110.2	148.2	149.6
12. Electricity Generation & Supply	102.2	125.1	146.7	166.6	196.9
13. Shipping	215.4	140.8	217.5	444.7	321.0
ALL INDUSTRIES	128.7	109.6	150.8	151.7	168.7

Note: "Gross Profits including depreciation" is the sum of profits before tax, managing agents' remuneration, interest charges and depreciation provision.

(*a*) Includes (1) Non-ferrous metals, (2) Transport equipment, (3) Electrical machinery and (4) Machinery (other than transport and electrical).

(*b*) Includes (1) Basic industrial chemicals, (2) Medicines and pharmaceuticals and (3) Other chemicals.

Source: *Reserve Bank of India Bulletin.*

APPENDIX X

INDEX OF PROFITS AFTER TAX

(Base 1950 = 100)

Industry	1951	1953	1955	1957	1958
I. *Plantation Industry* ..	63.2	123.6	82.1	55.0	70.8
1. Tea	53.2	142.6	69.3	50.7	82.7
2. Coffee	148.3	120.7	128.9	107.2	114.1
II. *Mining & Quarrying* ..	121.3	154.1	199.7	226 .2	291
3. Coal	96.1	76.4	135.4	119.4	148
III. *Processing & Manufacture—Foodstuffs, Textiles & Products thereof*	150.3	82.2	139.0	41.3	66.4
4. Vegetable Oils ..	—	218.4	374.7	—	242.7
5. Cotton Textiles ..	156.5	63.3	150.3	—	5.5
6. Jute Textiles	150.2	62.1	43.2	196.6	508.5
IV. *Processing & Manufacture—Metals, Chemicals, Minerals, etc.*	127.8	107.1	269.0	251.8	190.9
7. Iron & Steel	157.1	166.2	326.5	279.7	318.9
8. Engineering (*a*) ..	116.1	100.1	338.2	347.5	398.2
9. Chemicals (*b*) ..	96.7	29.8	162.1	183.0	226.2
10. Matches	96.2	92.3	88.4	37.2	104.6
V. *Processing & Manufacture—Not elsewhere classified* ..	154.4	125.8	165.4	200.4	215.0
11. Cement	119.9	114.3	151.8	124.8	102.2
VI. *Other Industries*	129.9	77.3	98.5	132.3	130.1
12. Electricity Generation and Supply	110.4	130.6	157.4	191.4	205.4
13. Shipping	723.3	157.0	409.0	2337.1	1112.5
ALL INDUSTRIES	131.6	98.1	149.8	116.4	114.4

NOTE: "Profits after Tax" is the difference between the profits before tax, which includes tax provision, dividends distributed and profits retained in the form of transfers to reserves (other than taxation and depreciation), and balance carried to balance sheet and tax provision.

(*a*) Includes (1) Non-ferrous metals, (2) Transport equipment, (3) Electrical machinery and (4) Machinery (other than transport and electrical).

(*b*) Includes (1) Basic industrial chemicals, (2) Medicines and pharmaceuticals and (3) Other chemicals.

Source: *Reserve Bank of India Bulletin.*

Appendix XI

PROFITS AFTER TAX AS PERCENTAGE OF NET WORTH

	750 Companies		1001 Companies		
	1951-55 Average	1956	57	1958	1959
Cotton Textiles	5.6	8.3	– 1.2	0.3	7.1
Jute Textiles	5.9	—4.2	3.3	7.8	12.6
Other Textiles	3.7	9.6	7.6	8.4	21.9
Iron and Steel	17.6	14.6	11.2	11.9	14.9
Engineering	6.4	9.7	9.5	9.3	11.4
Mineral Oils	—	28.8	16.7	14.7	15.5
Cement	11.0	10.4	7.3	5.3	8.1
Sugar	10.0	10.1	9.6	8.3	11.8
Paper	10.6	6.2	7.2	10.7	12.3
Vegetable Oils	—	4.0	—3.5	6.2	15.8
Chemicals	3.0	6.3	5.3	6.6	11.3
Matches	11.0	8.0	3.5	9.5	14.7
Coal	6.5	3.1	5.6	6.7	6.1
Electricity	7.3	6.8	7.9	8.1	8.4
Shipping	5.1	12.6	13.4	6.2	0.7
Tea Plantations	14.3	11.2	3.8	6.0	10.3
Other Plantations	14.0	13.8	9.1	9.8	7.4
Total (including others) ..	7.9	8.8	6.5	7.1	10.5

Source: *Reserve Bank of India Bulletin.*

APPENDIX XII

DIVIDEND RATES

(Dividends on equity shares as percentage of Paid-up Capital)

	750 Companies		1001 Companies		
	1951-55 Average	1956	1957	1958	1959
Cotton Textiles	8.7	11.1	8.2	8.2	11.6
Jute Textiles	10.0	4.4	6.3	9.0	13.6
Other Textiles	3.1	4.7	4.7	8.8	16.3
Iron and Steel	15.2	9.3	9.2	7.7	12.5
Engineering	3.9	7.7	7.6	8.7	11.7
Mineral Oils	—	18.8	12.9	12.9	15.5
Cement	9.2	8.5	9.7	7.6	10.0
Sugar	11.5	12.2	11.9	13.6	16.5
Paper	10.9	10.9	11.2	12.6	15.5
Vegetable Oils	2.8	3.3	3.5	5.3	9.9
Chemicals	2.6	6.1	5.6	7.6	8.8
Matches	10.8	10.9	10.9	10.9	15.8
Coal	7.1	7.9	8.6	9.3	10.2
Electricity	6.9	6.4	7.4	7.6	8.1
Shipping	3.5	8.1	8.2	7.8	4.4
Tea Plantations	17.4	16.4	10.0	10.3	14.4
Other Plantations	16.1	20.2	15.3	14.8	12.9
TOTAL (including others) ..	8.2	9.4	8.7	9.0	11.8

Source: *Reserve Bank of India Bulletin.*

APPENDIX XIII

ALLOCATION OF PROFITS DURING 1946-1958

Source and Period	As % of Profits before Tax			As % of Profits after Tax		As % of Paid-up Capital	
	Tax Provision	Profits distributed	Profits retained	Profits distributed	Profits retained	Profits after tax	Profits distributed
A. *TEC Sample of 492 Companies*							
1946-51	44.0	32.0	23.0	57.7	40.1	15.2	7.7
B. *RBI Sample of 750 Companies*							
1951-55	40.7	36.3	22.9	61.3	38.7	12.2	7.4
C. *RBI Sample of 1,001 Companies*							
1955	42.7	32.7	24.4	57.2	42.7	15.2	8.7
1956	45.1	32.4	22.4	59.1	40.8	14.5	8.5
1957	48.0	39.3	12.6	75.7	24.2	10.5	8.0
1958	46.2	38.7	14.9	72.1	27.8	11.5	8.3
1959	36.3	39.6	23.7	62.5	37.4	17.3	10.8
Average for 1955-59	43.0	36.7	20.0	64.5	35.4	13.4	8.9

NOTE: (*a*) 'Profits before Tax' is the sum of tax provision, dividends distributed and profits retained in business in the form of transfers to reserves (other than taxation and depreciation) and balance carried to balance sheet.
(*b*) 'Profits after Tax' is the difference between profits before tax (as defined above) and tax provision.

Source: Prepared on the basis of data published in the *Reserve Bank of India Bulletins*.

APPENDIX XIV

FINANCIAL PARTICULARS RELATING TO 1340 MANAGING AGENCY FIRMS FUNCTIONING IN INDIA IN 1951-52

(Figures in lakhs of rupees)

State	No. of managed companies taken into account	Paid-up capital	Share capital subscribed by Managing Agents	Percentage of capital subscribed by Managing Agents.	Loans and advances made by Managing Agents.	Loans guaranteed by Managing Agents.	Loans from banks	Total Loans and advances	Loans and advances made or guaranteed by Managing Agents as % of total loans and advances
1. Andhra	53	1,62	25	15.43	32	2	1	35	97.14
2. Assam	15	12	1	8.33	1	5	2	8	75.00
3. Bihar	81	5,48	28	5.11	3	57	55	1,15	52.17
4. Bombay	589	1,22,91	21,79	17.73	3,76	1,14	34,04	38,94	12.58
5. Madhya Pradesh	45	1,03	19	18.45	7	5	15	27	44.44
6. Madras	331	26,62	1,26	4.73	61	1,07	5,61	7,29	23.05
7. Punjab	53	2,69	52	19.33	4	—	1,08	1,12	3.57
8. West Bengal	264	13,78	96	6.97	96	20	5,48	6,64	17.47
9. Hyderabad	41	9,18	1,61	17.54	2,62	3,34	4,00	9,96	59.84
10. Madhya Bharat	51	12,91	59	4.57	1,12	—	3,42	4,54	24.67
11. Mysore	41	2,54	23	9.06	36	53	81	1,70	52.35
12. Pepsu	17	2,09	18	8.61	—	—	42	42	—
13. Travancore-Cochin	50	7,80	28	3.59	28	21	31	80	61.25
14. Delhi	75	6,22	1,04	16.72	35	58	2,24	3,17	29.34
15. Ajmer	9	20	7	35.00	1	—	—	1	100.00
16. Tripura	5	2	1	50.00	—	—	—	—	—
Total	1,720	2,15,21	29,27	13.60	10,54	7,76	58,14	76,44	23.94

Source: *Department of Company Law Administration, New Delhi.*

Appendix XV

STATE-WISE DISTRIBUTION OF COMPANIES AT WORK

(1957-58)

(In lakhs of rupees)

	Number	Paid-up Capital	% to the total number	% to the total paid-up capital
Northern Region				
Punjab	862	17,27	3.0	1.3
Rajasthan	494	20,49	1.7	1.6
Uttar Pradesh	1,411	37,96	5.0	2.9
Delhi	1,440	1,98,50	5.1	15.2
Himachal Pradesh ..	9	63	—	—
TOTAL	4,216	2,74,85	14.8	21.0
Eastern Region				
Assam	365	5,42	1.3	0.4
Bihar	498	37,72	1.8	2.9
Orissa	195	8,69	0.7	0.7
West Bengal	12,249	3,49,73	43.4	26.8
Manipur	8	16	—	—
Tripura	12	25	—	—
Total	13,327	4,01,97	47.2	30.8
Western Region				
Bombay	5,546	4,23,86	19.6	32.4
Madhya Pradesh ..	439	28,60	1.5	2.2
Total	5,985	4,52,46	21.1	34.6
Southern Region				
Andhra Pradesh ..	524	21,79	1.9	1.7
Kerala	1,212	29,46	4.3	2.3
Madras	2,288	85,83	8.1	6.6
Mysore	728	39,92	2.6	3.0
Total	4,752	1,77,00	16.9	13.6
GRAND TOTAL	28,280	13,06,28	100.0	100.0

Source: *Department of Company Law Administration, New Delhi.*

APPENDIX XVI

STATE-WISE DISTRIBUTION OF NEW COMPANIES

(In lakhs of rupees)

States	1956-57		1957-58		1958-59		1959-60		1960-61	
	No.	Authorised Capital	No.	Authorised Capital	No.	Authorised Capital	No.	Authorised Capital	No.	Authorised Capital
West Bengal ..	301	16,64	359	20,90	364	17,40	399	33,90	431	59,61
Bombay ..	170	55,94	191	39,95	240	89,22	293	67,45	407*	1,12,46*
Madras ..	91	33,13	80	15,22	113	3,50	342	13,75	343	57,17
Other States ..	286	1,04,94	331	26,64	378	1,74,24	418	45,44	502	57,81
Total ..	848	2,10,65	961	1,02,71	1,095	2,84,36	1,452	1,60,54	1,683	2,87,05

* N. B. The Bombay figures for 1960-61 are for Maharashtra and Gujarat.
Source: *Department of Company Law Administration, New Delhi.*

Appendix XVII

LIST OF THE FIRST TEN OF THE BIGGEST COMPANIES AT WORK

A. *Ranked according to total tangible assets:*

Rank	Name of Company	Total tangible assets (net of depreciation) (Crores of Rs)
1.	Hindustan Steel, Ltd.	557.1
2.	Tata Iron & Steel Co., Ltd.	170.2
3.	Indian Iron & Steel Co., Ltd.	92.8
4.	Scindia Steam Navigation Co., Ltd.	45.1
5.	Associated Cement Companies Ltd.	43.9
6.	National Coal Development Corporation	38.5
7.	Burmah Shell Refineries Ltd.	38.4
8.	Sindri Fertilisers & Chemicals Limited	37.0
9.	Hindustan Aircraft	31.3
10.	Tata Engineering & Locomotive Co., Ltd.	31.2

Continued

APPENDIX XVII—*Concld.*

B. *Ranked according to total sales or income*[1]*:*

Rank	Name of Company	Total Sales or Income (Crores of Rs)
1.	Tata Iron & Steel Co., Ltd.	86.7
2.	Indian Iron & Steel Co., Ltd.	48.0
3.	State Trading Corporation	42.8
4.	Hindustan Lever Limited.	41.9
5.	Imperial Tobacco Co., Ltd.	36.9
6.	Delhi Cloth & General Mills	30.1
7.	Standard Vacuum Refining Co.	29.7
8.	Tata Engineering & Locomotive Co., Ltd.	28.3
9.	Dunlop Rubber Co. (India) Ltd.	25.9
10.	Associated Cement Companies Ltd.	25.6

[1]N.B. (*a*) The ranking is as on March 31, 1961.

(*b*) Excludes banking and insurance companies.

Source: *Department of Company Law Administration, New Delhi.*

Appendix XVIII

SIZE PATTERN OF NEW COMPANIES

Size group according to authorised capital	1957-58	1958-59	1959-60	1960-61	Total
Below Rs. 1 lakh	231	252	346	370	1,199
Rs. 1 lakh to under Rs 5 lakhs	374	442	549	566	1,931
Rs. 5 lakhs to under Rs. 10 lakhs	229	274	334	381	1,218
Rs. 10 lakhs to under Rs. 25 lakhs	66	63	122	177	428
Rs. 25 lakhs to under Rs. 50 lakhs	24	24	36	47	131
Rs. 50 lakhs to under Rs. 1 crore	9	18	34	53	114
Rs. 1 crore and above ..	28	22	31	89	170
Total	961	1,095	1,452	1,683	5,191

Source: *Department of Company Law Administration, New Delhi.*

Appendix XIX

COMPANIES AT WORK IN EACH PAID-UP CAPITAL GROUP AS ON MARCH, 1958

(In lakhs of rupees)

Size-Group	Public		Private		Total	
	No.	Paid-up Capital	No.	Paid-up Capital	No.	Paid-up Capital
Below Rs. 5 lakhs ..	6,251	56,10	18,572	1,04,95	24,823	1,61,05
Rs. 5 lakhs to below Rs. 10 lakhs ..	752	50,71	849	50,22	1,601	1,00,93
Rs. 10 lakhs to below Rs. 25 lakhs ..	699	1,05,81	376	51,18	1,075	1,56,99
Rs. 25 lakhs to below Rs. 50 lakhs ..	288	97,25	111	36,54	399	1,33,79
Rs. 50 lakhs to below Rs. 75 lakhs ...	128	76,57	30	16,93	158	93,50
Rs. 75 lakhs to below Rs. 1 crore ..	59	49,97	9	7,43	68	57,40
Rs. 1 crore and above ..	119	3,37,16	37	2,65,46	156	6,02,62
Total ..	8,296	7,73,57	19,984	5,32,71	28,280	13,06,28

Source: *Department of Company Law Administration, New Delhi.*

Appendix XX

WORLD'S TOP* INDUSTRIAL GIANTS

Name of Company	Country of Origin	Total sales (Rs) (crores)	Total assets (Rs) (crores)
1. General Motors	U.S.A. ..	6,064	4,071
2. Standard Oil (N.J.) ..	U.S.A. ..	3,827	4,803
3. Royal Dutch/Shell ..	U.K./Holland ..	2,608	4,236
4. Ford Motors	U.S.A. ..	2,494	1,918
5. General Electric ..	U.S.A. ..	1,999	1,214
6. Unilever	U.K./Holland ..	1,847	1,076
7. U.S. Steel	U.S.A. ..	1,761	2,275
8. Socony Mobiloil ..	U.S.A. ..	1,514	1,645
9. Chrysler	U.S.A. ..	1,431	652
10. Texaco	U.S.A. ..	1,418	1,737
11. British Petroleum ..	U.K.	862	962
12. Imperial Chemical Industries	U.K.	743	1,100
13. Nestles	Switzerland ..	725	114
14. Philips	Holland ..	595	688
15. Volkswagenwerk A.G. ..	West Germany ..	524	257
16. Fried Krupp	West Germany ..	466	N.A.
17. British Motors	U.K.	461	200
18. Siemens	West Germany ..	460	386

*N.B. The ranking is as in 1960.

Source: *FORTUNE* (U.S.A.), August, 1961.

APPENDIX XXI

GOVERNMENT AND NON-GOVERNMENT COMPANIES AT WORK

(In crores of rupees)

Year ending	Govt. Companies		Non-Govt. Companies		Total	
	No.	Paid-up Capital	No.	Paid-up Capital	No.	Paid-up Capital
31.3.1956	61	66.0	29,813	9,58.2	29,874	10,24.2
31.3.1957	74	72.6	29,283	10,05.0	29,357	10,77.6
31.3.1958	91	2,56.8	28,189	10,49.5	28,280	13,06.3
31.3.1959	103	4,24.2	27,376	10,85.6	27,479	15,09.8
31.3.1960	125	4,68.4	26,796	11,24.7	26,921	15,93.1
31.3.1961	139	4,98.4	25,969	12,26.2	26,108	17,24.6

Source : *Department of Company Law Administration, New Delhi.*

APPENDIX XXII

MANAGING AGENCY REMUNERATION AS PERCENTAGE OF PROFITS BEFORE TAX

Year	No. of companies to which the financial results relate	Profits before tax (inclusive of managing agency remuneration)	Managing agency remuneration paid by companies to managing agents	Percentage of managing agency remuneration to the profits before tax.(col. 4 as% of col. 3)
(1)	(2)	(3)	(4)	(5)*
1955	744	98.43	14.09	14.2
1956	745	89.02	11.52	11.5
1957	693	63.60	8.38	11.6
1958	668	77.82	8.81	10.2

* N.B. The percentages in col. 5 have been worked out from the actual figures of managing agency remuneration and profits before tax, and not from the rounded figures given in cols. 3 and 4.

Source : *Department of Company Law Administration, New Delhi.*

Appendix XXIII

DEBT POSITION OF THE GOVERNMENT OF INDIA

(In crores of rupees)

Year ending March	Undated	Over 10 years	Betwen 5 & 10 years	Under 5 years	Total Internal Debt	Total External Debt
1948	257.74	682.42	285.62	287.23	1,513.01	49.40
1949	257.86	711.59	196.90	309.80	1,476.15	42.84
1950	257.85	597.93	303.08	291.08	1,449.94	56.50
1951	257.85	519.33	342.51	318.77	1,438.46	49.81
1952	257.85	463.47	450.14	232.05	1,403.51	136.99
1953	257.85	387.60	411.67	346.46	1,403.58	138.53
1954	257.85	271.43	546.93	288.06	1,364.27	136.44
1955	257.85	241.14	621.70	353.70	1,474.39	133.20
1956	257.85	241.17	616.52	393.13	1,508.67	138.81
1957	257.85	245.83	665.43	464.50	1,633.61	160.98
1958	257.85	259.08	625.22	557.35	1,699.50	211.02
1959	257.85	606.41	596.84	719.87	2,180.96	391.35
1960	257.85	707.48	662.38	810.53	2,438.23	630.50
1961	257.85	691.67	755.19	866.62	2,571.33	846.22

Note: Treasury Bills and Small Savings have been excluded from the above.
Source: *Report on Currency and Finance in India, Reserve Bank of India.*

Appendix XXIV

GROWTH OF SMALL SAVINGS IN INDIA

(In crores of rupees)

Year	Amount
1951-52	38.5
1952-53	40.2
1953-54	37.8
1954-55	55.1
1955-56	66.5
1956-57	59.0
1957-58	69.4
1958-59	78.2
1959-60	82.8
1960-61	100.0

Note: The figures are of net savings arrived at by deducting the amounts withdrawn or certificates encashed from the total gross receipts.
Source: *Budgets of the Central Government of India.*

Appendix XXV

VOLUME AND PATTERN OF SAVINGS

(In crores of rupees at 1948-49 prices)

	1950-51	1951-52	1952-53	1953-54	1954-55	1955-56	1956-57	1957-58	As proportion (per cent) of Total Savings during 1950-51 to 1957-58	House-hold Sector's savings during 1950-51 to 1957-58	National Income during 1950-51 to 1957-58	Annual Average (per cent) Rate of Growth during 1950-51 to 1957-58
1. Government Sector ..	91	162	65	22	38	28	89	99	11.0	..	0.7	—5.3
(a)	(15.0)	(35.2)	(11.5)	(4.1)	(5.6)	(3.3)	(9.4)	(13.2)				
(b)	(1.0)	(1.8)	(0.7)	(0.2)	(0.4)	(0.3)	(0.8)	(1.0)				
2. Domestic Corporate Sector	35	60	7	25	49	68	56	16	5.8	..	0.4	3.8
(a)	(5.7)	(13.1)	(1.2)	(4.7)	(7.2)	(7.9)	(5.9)	(2.1)				
(b)	(0.4)	(0.7)	(0.1)	(0.3)	(0.4)	(0.6)	(0.5)	(0.1)				
3. Household Sector ..	481	237	493	490	595	758	805	638	83.2	100.0	5.7	4.8
(a)	(79.3)	(51.7)	(87.3)	(91.2)	(87.2)	(88.8)	(84.7)	(84.7)				
(b)	(5.5)	(2.6)	(5.2)	(4.9)	(5.8)	(7.2)	(7.3)	(5.9)				
(i) Rural Household Sector	177	178	180	197	181	184	209	197	27.8	33.4	1.9	1.8
(a)	(29.1)	(38.8)	(31.8)	(36.7)	(26.5)	(21.6)	(21.9)	(26.2)				
(b)	(2.0)	(2.0)	(1.9)	(2.0)	(1.8)	(1.8)	(1.9)	(1.8)				
(c)	(36.7)	(75.0)	(36.5)	(40.3)	(30.4)	(24.3)	(25.9)	(30.9)				

Continued.

	1950-51	1951-52	1952-53	1953-54	1954-55	1955-56	1956-57	1957-58	As proportion (per cent) of Annual: Total Savings during 1950-51 to 1957-58	House-hold Sector's Savings during 1950-51 to 1957-58	Nationl Incomea during 1950-51 to 1957-58	Average (per cent) Rate of Growth during 1950-51 to 1957-58
(ii) Urban Household Sector	304	59	313	293	414	574	596	441	55.4	66.6	3.8	6.6
(*a*)	(50.2)	(12.9)	(55.5)	(54.5)	(60.7)	(67.2)	(62.8)	(58.5)				
(*b*)	(3.5)	(0.6)	(3.3)	(2.9)	(4.0)	(5.4)	(5.4)	(4.0)				
(*c*)	(63.3)	(25.0)	(63.5)	(59.7)	(69.6)	(75.7)	(74.1)	(69.0)				
4. Total Savings (1+2+3)	607	459	565	537	682	854	950	753	100.0	..	6.8	3.3
Total Savings as proportion (per cent) of National Income	6.9	5.1	6.0	5.4	6.6	8.1	8.6	7.0				

	Average Saving-Income Ratio	Marginal Saving-Income Ratio
1951-52 to 1957-58 ..	6.7	7.4

Figures have been rounded off to the nearest crore.
a : Proportion (per cent) of Total Savings; *b* : Proportion (per cent) of National Income; *c* : Proportion (per cent) of Savings of the Household Sector.
Source : *Reserve Bank of India Bulletin, March 1960.*

APPENDIX XXVI

VOLUME AND PATTERN OF SAVINGS OF THE HOUSEHOLD SECTOR

(In crores of rupees at 1948-49 prices)

	1950-51	1951-52	1952-53	1953-54	1954-55	1955-56	1956-57	1957-58	As proportion (per cent) of Household Sector's Savings during 1950-51 to 1957-58	As proportion (per cent) of National Income during 1950-51 to 1957-58	Annual Average (per cent) Rate of Growth during 1950-51 to 1957-58
1. Currency	78	–106	–17	29	70	216	48	42	8.0	0.5	–12.1
(a)	(16.3)	(--44.6)	(–3.4)	(5.9)	(11.7)	(28.6)	(5.9)	(6.6)			
(b)	(0.9)	(–1.1)	(–0.2)	(0.3)	(0.7)	(2.1)	(0.4)	(0.4)			
2. Net Bank Deposits	–2	–40	24	—	10	31	–3	–16	0.1	0.01	–37.6
(a)	(–0.4)	(-16.9)	(5.0)	—	(1.7)	(4.0)	(–0.4)	(–2.4)			
(b)	(—)	(–0.4)	(0.3)	—	(0.1)	(0.3)	—	(–0.1)			
3. Gold	19	32	18	12	12	13	22	31	3.6	0.2	1.7
(a)	(3.9)	(13.4)	(3.6)	(2.6)	(2.1)	(1.7)	(2.8)	(4.8)			
(b)	(0.2)	(0.4)	(0.2)	(0.1)	(0.1)	(0.1)	(0.2)	(0.3)			

Continued.

	1950-51	1951-52	1952-53	1953-54	1954-55	1955-56	1956-57	1957-58	As proportion (per cent) of Household Sector's Savings during 1950-51 to 1957-58	As proportion (per cent) of National Income during 1950-51 to 1957-58	Annual Average (per cent) Rate of Growth during 1050-51 to 1957-58
4. Insurance Policies	7	22	17	20	25	15	34	15	3.4	0.2	49.7
(a)	(1.5)	(9.1)	(3.4)	(4.0)	(4.1)	(2.0)	(4.3)	(2.3)			
(b)	(0.1)	(0.2)	(0.2)	(0.2)	(0.2)	(0.1)	(0.3)	(0.1)			
5. Provident Funds	27	35	39	51	64	69	71	74	9.6	0.5	27.6
(a)	(5.7)	(14.8)	(7.9)	(10.4)	(10.8)	(9.1)	(8.8)	(11.7)			
(b)	(0.3)	(0.3)	(0.4)	(0.5)	(0.7)	(0.7)	(0.6)	(0.7)			
6. Net Claims on the Government Sector (i.e. Government bonds etc.)	16	21	24	30	35	53	54	43	6.2	0.4	33.5
(a)	(3.3)	(9.0)	(4.9)	(6.2)	(5.9)	(7.0)	(6.8)	(6.7)			
(b)	(0.2)	(0.2)	(0.3)	(0.3)	(0.4)	(0.5)	(0.5)	(0.4)			

Continued.

	1950-51	1951-52	1952-53	1953-54	1954-55	1955-56	1956-57	1957-58	As proportion (per cent) of Household Sector's Savings during 1950-51 to 1957-58	As proportion (per cent) of National Income during 1950-51 to 1957-58	Annual Average (per-cent) Rate of Growth during 1950-51 to 1957-58
7. Corporate Shares and Securities	17	–5	4	17	15	1	61	29	3.0	0.2	0.9
(*a*)	(3.4)	(–1.9)	(0.7)	(3.4)	(2.4)	(0.1)	(7.5)	(4.5)			
(*b*)	(0.2)	(–0.1)	—	(0.2)	(0.1)	—	(0.6)	(0.3)			
8. Physical Assets	319	278	384	331	364	360	518	420	66.1	3.7	4.8
(*a*)	(66.3)	(117.1)	(77.9)	(67.5)	(61.3)	(47.5)	(64.3)	(65.8)			
(*b*)	(3.6)	(3.1)	(4.0)	(3.3)	(3.5)	(3.4)	(4.7)	(3.8)			
9. Savings of the Household Sector (1 to 8)	481	237	493	490	595	758	805	638	100.0	5.7	4.8
(*b*)	(5.5)	(2.6)	(5.2)	(4.9)	(5.8)	(7.2)	(7.3)	(5.9)			

Figures have been rounded off to the nearest crore.
a: Proportion (per cent) of Household Sector's Savings; *b*: Proportion (per cent) of National Income. — = Negligible.
Source: *Reserve Bank of India Bulletin, March 1960.*

Appendix XXVII

INDEX OF INDUSTRIAL PRODUCTION

(Base: 1951–100)

Item	1954	1956	1958	1959	1960	1961 (Dec.)
I. *Mining & Quarrying:*	107.2	115.0	133.7	142.0	159.8	181.9
1. Coal ..	107.2	114.9	132.2	137.1	150.9	168.1
II. *Manufacturing:*						
2. Sugar ..	97.4	166.5	175.6	186.8	228.7	515.8
3. Cotton Textiles..	110.9	117.5	108.9	111.5	115.4	121.9
4. Jute Textiles ..	107.3	127.3	123.9	125.4	126.9	137.5
5. Paper & Paper Boards ..	117.7	146.6	191.8	222.9	257.6	273.0
6. Matches ..	91.5	106.6	108.3	112.3	114.5	136.3
7. Sulphuric Acid..	141.1	154.5	211.9	273.2	331.7	419.1
8. Cement ..	137.6	154.2	189.9	213.6	241.4	272.0
9. Iron & Steel ..	113.2	119.4	119.1	163.1	208.8	285.5
10. Aluminium ..	127.0	168.9	212.6	448.2	472.2	613.9
11. Sewing Machines	180.4	293.3	461.5	568.2	665.3	821.4
12. Electric Lamps..	148.7	198.0	196.4	224.5	266.7	320.1
13. Automobiles ..	64.9	144.3	120.3	163.8	232.0	244.3
14. Bicycles ..	325.8	581.0	798.6	867.0	919.5	1000.2
III. *Electricity, Gas & Steam* ..	127.0	164.1	209.0	248.5	280.1	352.7
General Index ..	112.9	132.6	139.7	151.9	170.3	198.9

Note: General Index is not adjusted for seasonal variations.
Source: *Monthly Statistics of the Productions of Selected Industries of India.*

Appendix XXVIII

INDEX OF PRODUCTIVITY OF LABOUR IN INDUSTRIES IN INDIA

Base: 1953—100

Year	Index of Productivity
1948	88.0
1949	88.1
1950	91.6
1951	105.4
1952	107.6
1953	100.0
1954	116.1
1955	132.9
1956	129.1
1957	130.4
1958	133.0

Source: Estimated on the basis of information contained in the Reports of Census of Indian Manufactures.

Appendix XXIX

SAVINGS DEPOSITS OF INDIAN JOINT STOCK BANKS*

End of	Savings Deposits (In crores of Rs)
1950	144.99
1951	146.69
1952	144.91
1953	147.24
1954	155.59
1955	171.14
1956	193.16
1957	204.50
1958	222.07
1959	246.54
1960	267.15

* Inclusive of scheduled and non-scheduled banks.

Source: *Statistical Tables Relating to Banks in India.*

Appendix XXX

ADVANCES OF SCHEDULED BANKS BY PURPOSE

(In crores of rupees)

Sector	Sept. 30, 1955		Oct. 31, 1957		Oct. 31, 1959		Oct. 31, 1960	
	Amount Rs	% distribution	Amount Rs	% distribution	Amount Rs	% distribution	Amount Rs	% distribution
Industry	215.7	35.2	383.7	43.6	418.5	44.7	562.8	51.2
Commerce	296.8	48.4	375.9	42.7	373.6	39.9	395.2	35.9
Agriculture	12.1	2.0	24.2	2.7	25.7	2.7	6.6	0.6
Personal & Professional	54.3	8.8	61.4	7.0	78.0	8.4	96.8	8.8
All others	34.6	5.6	35.4	4.0	40.0	4.3	38.6	3.5
TOTAL	613.5	100.0	880.6	100.0	935.8	100.0	1100.0	100.0

Source: *Trend and Progress of Banking in India.*

APPENDIX XXXI

ANALYSIS OF L.I.C. INVESTMENTS

(In Debentures, Preference Shares and Ordinary Shares)

among important Industries

(In crores of rupees)

Industries	End-1958		End-1959		End-1960	
	Amount Invested	% to total	Amount Invested	% to total	Amount Invested	% to total
1. Electricity ..	8.74	11.5	9.20	11.3	9.55	10.4
2. Engineering ..	8.69	11.4	9.73	11.9	9.10	9.9
3. Cotton ..	7.59	10.0	7.59	9.3	8.57	9.3
4. Iron & Steel ..	5.67	7.4	6.84	8.4	7.67	8.3
5. Jute ..	4.19	5.5	4.25	5.2	4.32	4.7
6. Cement ..	4.31	5.7	4.48	5.5	5.34	5.8
7. Paper & Pulp ..	3.11	4.1	3.24	4.0	4.09	4.4
8. Banks ..	2.86	3.8	2.99	3.7	2.97	3.2
9. Coal ..	1.97	2.6	2.24	2.7	2.36	2.6
10. Sugar & Breweries ..	1.71	2.2	1.79	2.2	2.90	3.2
11. Insurance ..	1.61	2.1	1.60	2.0	2.60	2.8
12. Plantations ..	0.42	1.9	1.66	2.0	2.00	2.2
13. Shipping & other transport ..	1.49	2.0	2.29	2.8	0.96	1.0
14. Chemicals & pharmaceuticals ..	1.28	1.7	1.76	2.2	1.83	2.0
15. Others ..	21.53	28.3	21.92	26.8	27.79	30.2
TOTAL ..	75.17	100.2	81.58	100.0	92.05	100.0

Source: *Report and Accounts of the Life Insurance Corporation of India.*

APPENDIX XXXII

NATIONAL INCOME OF INDIA BY SECTORS

(In crores of rupees)

Sector		1951-52	1953-54	1955-56	1957-58	1958-59	1959-60	1960-61
I. Agriculture, Animal husbandry, etc.	(a)	50.2	53.1	45.2	52.8	62.4	62.1	68.6
	(b)	44.4	49.8	50.2	50.1	55.6	55.0	58.6
II. Commerce. Transport & Communications.	(a)	17.9	18.0	18.8	20.7	21.5	22.4	23.6
	(b)	17.3	18.3	19.7	21.1	21.9	22.7	24.5
III. Mines, Manufacturing & Small enterprises.	(a)	16.8	17.7	18.5	21·2	21.7	23.3	26.4
	(b)	15.2	16.5	17.6	18.6	18.8	19.7	21.1
IV. Other Services.	(a)	15.0	16.0	17.3	19.3	20.6	21.9	23.8
	(b)	14.3	15.7	17.3	19.2	20.4	21.4	23.1
V. Net earned income from abroad.	(a)	–0.2	0.0	0.0	–0.1	–0.2	–0.3	–0.4
	(b)	–0.2	0.0	0.0	–0.1	–0.2	–0.3	–0.4
National Income	(a)	99.7	104.8	99.8	113.9	126.0	129.4	142.0
	(b)	91.0	100.3	104.8	108.9	116.5	118.5	126.9

NOTE: (a) At current prices.
(b) At 1948-49 prices.

Source: *Estimates of National Income published by the Central Statistical Organisation, Government of India.*

Appendix XXXIII

TOTAL DOMESTIC CAPITAL FORMATION IN INDIA

(In crores of rupees at 1948-49 prices)

Year (1)	Estimates of Capital formation (Rs) (2)	National income (Rs) (3)	Percentage of col 2 to col 3 (4)
1950-51	591	8,850	6.6
1951-52	460	9,100	5.0
1952-53	564	9.460	5.9
1953-54	573	10,030	5.7
1954-55	731	10,280	7.1
1955-56	955	10,480	9.1
1956-57	966	11,000	8.7
1957-58	782	10,890	7.1
1958-59	902	11,650	7.7
Annual Average between 1950-51 & 1958-59 ..	725	10,193	7.1

Source : *Reserve Bank of India Bulletin.*

Appendix XXXIV

INVESTMENTS IN INDUSTRIES, MINERALS AND ELECTRIC POWER IN THE THREE PLANS

(In crores of rupees)

	First Plan		Second Plan		Third Plan	
	Public Sector	Private Sector	Public Sector	Private Sector	Public Sector	Private Sector
Large-scale Industries & Minerals ..	60	340(*a*)	870	675(*a*)	1,520	1,050(*a*)
Electric Power ..	260	30	445	40	1,012	50
Total ..	320	370	1,315	715	2,532	1,100

(*a*) : Inclusive of investments on expansion, replacement and modernisation.
Source : *The Planning Commission.*

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